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ON

ENGLISH AND FOREIGN BANKING

AND

CURRENCY SYSTEMS

AND

FOREIGN EXCHANGES

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BY

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PREFACE

THE three articles "Banking," "Foreign Banking," and "Foreign Exchanges," which compose this little work, were originally written for the *Encyclopædia of Accounting*, now being issued by the publishers.

It was, however, pointed out to them that the articles were worthy of a much wider circulation than could hope to be attained by such an expensive work as the *Encyclopædia*.

Moreover, although written in the first place for professional men, they appeal specially to students of "Banking and Currency" and "Machinery of Business," as containing such an amount of thoroughly reliable and up-to-date information as is not to be found elsewhere within the same compass; while those students who aim at passing the examinations of the Bankers' Institute, the London Chamber of Commerce, and kindred institutions will find them a most valuable aid to success.

January 1904.

BANKING

By ERNEST SYKES, B.A. Oxon.

Banking

History.—As early as the eleventh and twelfth centuries the practice of banking had reached a highly developed state in the Italian cities and afterwards in the Low Countries; but if we except the usurers and the money-changers, we find no mention of it in England until the time of the Stuarts. In a pamphlet published in 1676 we find it stated: "Much about the same time, the goldsmiths (or new-fashioned bankers) began to receive the rents of gentlemen's estates remitted to town, and to allow them and others who put cash in their hands some interest for it. . . . This was a great allurement for people to put money in their hands, which would bear interest till the day they wanted it; and they could also draw it out by one hundred pounds, or fifty pounds, etc., at a time as they wanted it."

This was the beginning of the system of credit which is now the foundation of all modern business as well as of banking. But national public credit was, as yet, but precarious in the extreme. The king was still supposed to live "of his own," and his debts were secured by his personal good faith alone. When, therefore, Charles II., to whom the goldsmiths had lent large sums, closed the Exchequer in 1672 and confiscated £1,300,000 of the latter's money, public credit received a rude shock. The accession of William III., however, witnessed an entire change in this respect, and the personal sovereignty of the monarch gave way finally to the present system of parliamentary control and responsibility. William's foreign ambitions forced him into the hands of the Whigs, to whom he looked for his supplies. "They shall never be losers who trust to a parliamentary security," said he in a speech from the throne on 30th December 1701. When, therefore, Montague, the Chancellor of the Exchequer, adopted in 1694 the expedient suggested by a Scotsman named Patterson, of granting special banking facilities to a company in return for a loan to the State, the newly created public confidence was shown by the rapidity with which the capital of the "Bank of England" was subscribed. The establishment of the Bank of England was the foundation of our modern financial system; and by means of familiarising the public with the use of credit in productive enterprise, it opened up roads to wealth hitherto undreamt of. The bank was enabled to lend money at a much lower rate of interest than that charged by the goldsmiths, owing to their larger capital and the remunerative terms of their contract with the Government, and often discounted bills at 4 per cent instead of the 6 or 8 charged by their rivals.

But we must be careful to notice that although the bank received deposits and discounted bills, it was to their note issue that they attached primary importance and most jealously guarded. Therefore, in 1708, at one of the periodical renewals of their charter, we find a clause inserted (7 Anne, c. 7), granting them a monopoly in this respect: "During the

continuation of the said corporation of the Governor and Company of the Bank of England, it shall not be lawful for any body politic or corporate whatsoever . . . *exceeding the number of six persons*, in that part of Great Britain called England, to borrow, owe, or take up any sum or sums of money on their bills or notes, payable at demand, or at a less time than six months from the borrowing thereof."

This clause, which, be it noted, did not extend to Scotland, had a far-reaching effect, and put great obstacles in the way of the evolution of a class of powerful and responsible banks in England. Owing to the importance generally attached to the issue of notes, a conception arose that it was not possible to found other banking companies possessing adequate capital with any chance of success, so that for more than a century the Bank of England was without a rival except for private banking firms. Several of these were highly respectable houses, and have survived to the present day, notably Messrs. Child and Messrs. Hoare, both older than the Bank of England; but many of them possessed utterly inadequate resources, and collapsed with the first strain thrown upon them. The Bank of England survived all the panics of the eighteenth century without much difficulty, until the troubled times of the Napoleonic era; then in 1797, under the double stress of a drain set up by the country bankers, caused by fears of a French invasion, and the constant calls made upon its resources by Pitt, it was reduced to extremities, and the Government found it necessary to step in and forbid payments in cash except under certain rigid restrictions. The result was that gold was rapidly driven out of the ordinary channels of circulation, and the standard of value was no longer gold but a fictitious paper one. The curious phenomenon was experienced of a rise in the market price of gold bullion to £4:13s. per oz., that is to say, while gold was coined at the rate of £3 : 17 : 10½ per oz., the market price of an ounce of gold was £4 : 13s. The difference between these two prices was the measure of the depreciation of the paper currency—Bank of England and country bank notes. For a while the Government refused to admit the existence of this depreciation, and the celebrated report of the Select Committee of the House of Commons in 1811, commonly known as the "Bullion Report," which clearly showed the extent of the evil, was thrown out by a large majority of the House. This report was a masterly and forcible exposition of the principles which should govern the issue of a paper currency, and the errors in it are wonderfully few considering the fluctuating state of the general opinion on the subject. Succeeding events thoroughly justified the position taken up by its authors, and a violent contraction of the paper issues in the years 1814-16, owing to an acute monetary panic, restored the market price of bullion to its normal level. During the years 1821-23 payments in cash were gradually resumed, and owing chiefly to the exertions of Mr. Robert Peel the old standard rate of £3 : 17 : 10½ per oz. was maintained in defiance of a minority who proposed "that the Mint price of gold be altered to correspond with the market price" (Amendment of Lord Lauderdale to 59 Geo. III. c. 49).

The Bank of England had reason to congratulate itself on the way it had come through the ordeal of the suspension. It learnt the lesson that an unlimited issue of paper which is not payable in gold on demand cannot retain its value for long, however much it may be bolstered up by legislative enactment, and it learnt its lesson well. England has never since that time experienced the evils of an inconvertible paper currency, although most of her neighbours have, from time to time, succumbed to temptation and tasted the sweets and bitters of such a course. But although the Bank

of England had retrieved its reputation, so much can hardly be said of the country banks. Each recurring panic absorbed its tale of victims from their ranks, and the want of more reliable provincial banks forced itself on public attention. With the intent to remedy the evil the Bank of England was recommended by the Government to open branches in the provinces, and a start was made at Swansea, Gloucester, and Manchester. Negotiations were opened with the Governors of the Bank to induce them to modify the monopoly conferred on them by the charter of 1708, and an Act was passed (7 Geo. IV. c. 46) allowing the establishment of banks with more than 6 partners, provided they had no office within 65 miles of London, and their notes were not payable within such a radius. This was followed in 1833 by an explanatory clause, inserted in 3 and 4 Will. IV. c. 98, permitting the establishment of joint-stock banks in London without the privilege of a note issue. This significant clause marks a great change in the character of English banking. From this time forward the function of issuing notes dwindles into insignificance compared with the practice of deposit banking. What may be called the "habit" of banking now gained ground rapidly, and the local bank superseded the old stocking among all classes of Englishmen. England had, since the closing decades of the eighteenth century, assumed the position of the leading industrial nation of the world. The great business centres of the North and Midlands of England were being opened up, and England needed capital. This was largely supplied by the deposits of the new banks; deposits perhaps small individually, but mounting up in the aggregate to many millions. In no country of Europe has this "habit" of banking taken such firm root, and it must be reckoned as an important factor in our national development. Many of the leading joint-stock banks of to-day were the direct outcome of this clause of the Act of 1833, notably the London and Westminster Bank founded in 1834, the London Joint Stock Bank in 1836, and the Union Bank and the London and County Bank in 1839.

Bank Charter Act 1844.—This revival in banking was followed by an attempt to impose such legal restrictions on the Bank of England and the country banks as should prevent the occurrence of the monetary crises which caused such devastation at intervals, and also should ensure the convertibility of their note issues. These restrictions were embodied in the Bank Charter Act of 1844, introduced by Sir Robert Peel, and generally known as the "Bank Act." That the supporters of the bill had this twofold object in view is undoubted. Peel's own words, when the House went into Committee on the bill, are decisive as to his hopes of preventing these panics: "Some apprehend," says he, "that the proposed restrictions upon issue will diminish the power of the bank to act with energy at the period of monetary crises and commercial alarm and derangement. But the object of the measure is to prevent (so far as legislation can prevent) the recurrence of those evils from which we suffered in 1825, 1836, and 1839. It is better to prevent the paroxysm than to excite it and trust to desperate remedies for the means of recovery." The other important point to observe about this measure is that the dangers arising from improvident speculation and inflated prices are attributed by the great majority of the speakers to the action of bank notes alone, to the entire exclusion of such other instruments of credit as cheques and bills of exchange. The most important clauses of the Act are as follows:—

(1) The issue department of the Bank of England was to be kept wholly distinct from the banking department.

(2) The issue department was allowed to issue notes to the value of

£14,000,000 on securities; all notes issued in excess of this amount were to be secured by the deposit of bullion to an equal amount in the issue department.

(3) Of the bullion deposited in the issue department as security for notes, not more than one quarter was to consist of silver.

(4) Any one may demand notes from the issue department in exchange for gold, at the rate of £3 : 17 : 9 per oz.

(5) If at any time the authorised issue of any bank shall lapse in accordance with the provisions of this Act, the Bank of England may increase the securities in the issue department against which notes are issued, to the extent of two-thirds of such issue, with the permission of Her Majesty in Council.

(6) The Bank of England to publish a weekly account of the notes, bullion, securities, and deposits in both departments.

(10) No new bank of issue to be created.

(11) It shall not be lawful for any company or partnership, now consisting of only six or less than six persons, to issue bank notes at any time after the number of partners shall exceed six in the whole.

(12) Bankers ceasing to issue, or becoming bankrupt, may not resume the power of issue.

(13) Existing banks of issue not to exceed their average circulation for the twelve weeks preceding 27th April 1844.

(18) Every bank of issue to render to the Comptroller of Stamps and Taxes a weekly account of his daily circulation, and a monthly account of his average for the month.

Much controversy has been aroused as to the good or evil effects of the Bank Act of 1844. Certainly it failed in some of the expectations of its supporters, for the country has suffered from successive severe panics in 1847, 1857, 1866, and 1877, and the Act has had to be suspended in each of the three first-mentioned years, so as to allow of the issue of notes in excess of the limit without the deposit of bullion. The Act has neither secured us against seasons of intense monetary pressure and lack of public confidence, nor has it ensured the convertibility of the Bank of England note. Its supporters forgot that the liabilities of the bank to pay gold on demand are not confined to those arising from its note circulation. Every amount credited in the books of the Bank of England to any of its banking customers is a fresh liability incurred by the bank, and the reserve of coin is open to a drain from this quarter just as much as from the presentation of bank notes; the whole of the metallic reserve of the Bank of England might easily be drawn out by the cheques of its customers, which include all the leading joint-stock banks, without the note circulation being contracted to the extent of a single note. When this reserve is gone, there remains the bullion which is held in the issue department as security for notes issued beyond £14,000,000; this stock of bullion must then either be used for banking purposes, that is to say, in payment of cheques and in advances to other banks, in which case the convertibility of the bank note would no longer be assured, or else the whole of the banking system of the country must collapse. The Bank of England is the pivot round which revolves the whole of our banking system, and it holds the ultimate reserve on which rests the credit of the country: therefore, if this last stock of bullion must be retained in order to render the convertibility of the note absolutely assured, the whole of the national credit may have to be sacrificed.

As a matter of history the Bank Charter Act, so far as it affects the

convertibility of the Bank of England note, is rapidly becoming obsolete and unnecessary. The danger of a possible collapse of credit lies now almost entirely in the direction of the purely banking business of the country and not in the note issue. The issue of notes by the Bank of England tends to become stereotyped and automatic, and the amount varies chiefly according to the season of the year and such causes as can easily be foreseen. On the other hand, the enormous system of credit which characterises our present economic condition has become more delicate and complex than ever, and it rests on a comparatively slender basis of bullion; this is a fact to be accepted, and one which admits of no discussion; a return to cash payments would be impossible to-day; it may be that this renders our position one of continual insecurity, and dangles before our eyes the ever-present possibility of disaster, but it is a position from which we cannot retire. What we can do is to ensure that the Bank of England reserve is an efficient one, and it is by drawing attention to this fact that the Bank Act of 1844 has deserved most at our hands. The Bank reserve is still insufficient, and a wish has been urged in many quarters that the leading joint-stock banks might be induced to share the burden of keeping the bullion reserve with the Bank of England. It is pointed out that the Bank of England is a corporation of business men actuated by the hopes and fears incidental to dividend-paying and carrying on its business in competition with the leading joint-stock banks, and that its privilege of being the Government banker is not enough to justify the imposition on to its shoulders of the whole burden of keeping the national reserve. This argument derives strength from the fact that the last ten years of the nineteenth century have evolved a much more powerful class of bank than formerly existed. A passion, for amalgamation characterised these years, and under its influence most of the smaller joint-stock bankers and almost all of the private bankers have been absorbed by their more influential neighbours.

Since the year 1878 we have not suffered one of those monetary crises which had hitherto occurred so regularly at intervals of ten years. It is true that in 1890, when Baring Brothers were unable to meet their engagements, a panic might have occurred but for the promptitude with which the clearing bankers met and agreed to jointly guarantee the engagements of the defaulting firm. This freedom from panic is probably due to the increased experience and improved methods of the later generation of bankers, and perhaps also to the greater publicity with which banking and in fact nearly all financial business is now carried on. With the evolution of a more powerful type of bank has come an increased sense of responsibility and a dislike for running great risks. All bankers now realise the folly of granting large permanent overdrafts to single firms or individuals, and it is to be hoped that a repetition of the experiences of the City of Glasgow Bank would now be impossible. When that bank stopped payment in 1878 it was found that, with a capital of only £1,000,000, it had advanced no less than £6,000,000 to five firms, all of whom proved insolvent.

Scotch and Irish Banking.—Banking in Scotland has developed on somewhat different lines from those followed in England, and she has escaped many of the dangers and difficulties which have beset her southern neighbour. The Bank of Scotland was founded in the year following that of its prototype, with exclusive privileges of banking; but unlike those of the Bank of England, these privileges were not continued, and a rival, the Royal Bank of Scotland, was founded in 1727, followed in 1746 by the

British Linen Company, all of them being incorporated by Royal Charter. The Scotch banks opened branches in the provinces at a much earlier date than was the case in England, and the practice of banking quickly became established among the people. Scotch banks from as early as 1704 issued £1 notes, and have continued to do so till the present day, while in England none have been issued by the Bank of England since 1825. The result has been to accustom the people to the use of a paper currency to such an extent that a great economy has been effected in the use of gold, and the country has not experienced that rush for coin and distrust of all paper in times of panic which has caused such distress in England. This practice has been helped by the system of "cash-credits," which has played such a prominent part in the development of banking in Scotland. These cash-credits were loans issued on the security of two or more individuals, and repayable on demand, the borrower being credited with such sums, not exceeding the total amount of the cash-credit, as he required from time to time. These loans were of course made by means of the notes of the bank; and as these notes were payable at the head office of the bank only, it was but seldom that the branches were compelled to pay any large sums in gold.

It is easy to see that this system of banking, in which notes played such an important part, favoured the formation of powerful banks; and as there did not exist the legal restrictions which forbade the rise of such a class in England, the private bankers were unable to survive for long. To such an extent has this process been developed, that there are at the present time but ten banks in Scotland, all of them joint-stock institutions.

In Ireland the development of banking was upon lines similar to those of England. The Bank of Ireland was incorporated in 1782, with exclusive privileges of joint-stock banking. This monopoly was not relaxed until 1821, when an exception was made of those parts of Ireland which were more than fifty miles from Dublin. Consequently Ireland has suffered considerably from the insecurity attaching to small private banks; but the rise of the Provincial Bank of Ireland in 1826, followed by other joint-stock banks, resulted in their rapid decay, and there now remain no private banks in Ireland outside of Dublin.

The year 1845 saw the main principles of the Bank Charter Act of 1844 extended to Scotland and Ireland. In both of these countries the right to issue notes was finally restricted to those banks which had exercised the privilege during the year preceding 1st May 1845. The amount of each bank's issue was not to exceed the average amount during the above-mentioned year, together with an amount equal to the stock of bullion they may possess at the time, of which three-fourths must be gold.

The Practice of Banking.—Having given this brief sketch of the development of our banking system, we can now deal with practical banking as it is carried on at the present time.

A few words are necessary as to our currency. Our coinage is regulated by the Act of 1816, which first legally established our currency on a basis of gold monometallism. Until the beginning of the eighteenth century silver had been the standard metal, but during the eighteenth century it was superseded by gold, and this change was legally recognised in 1816. By this Act silver was made legal tender only to the amount of forty shillings, and the right to coin silver was reserved to the State. Any one taking gold to the Mint is legally entitled to receive sovereigns for it, coined at the rate of £3 : 17 : 10½ per oz., which is called the Mint price of gold. This right is very little used, however, and gold is in practice always taken to the Bank of England, who allow £3 : 17 : 9 an oz., the difference of

1½d. an oz. being their charge for the transaction. Worn gold coins are received at the Mint at their full value, unless the deficiency amounts to more than three grains; but Pre-Victorian gold coins are no longer legal tender, and when presented to a bank a charge of sixpence each coin is usually made. Silver is coined at the rate of 5s. 6d. the oz.; and as the present price of silver is about two shillings an oz., there is obviously a large profit on coining silver, and it is necessary to limit its quantity by reserving the right to the Government. This system reduces our silver coins to the condition of "tokens." Until the breakdown of the "Latin Union" in 1874, most of the nations of the Continent had a double or bimetallic standard of value. Under this system, any one could bring either gold or silver to the Mint and demand coins in exchange which were a legal tender at the ratio of 15½ to 1, but the rapid fall in the price of silver, which has gradually declined from 5s. an oz. to its present price, compelled them to abandon the system; and although a strong party has existed even in England in favour of a revival of the bimetallic standard of value, its efforts have been futile and now seem hopeless. A famine in gold, and consequent general fall in prices, was prophesied as the result of the demonetisation of silver, but this has happily been prevented by the large output of gold from the Rand, and gold now seems firmly established in Europe as the standard of value. Bronze coins are also "tokens," and are legal tender only to the value of one shilling. Bank of England notes were made legal tender in England by the Act of 1844, except when tendered by the bank or its branches.

Banking we may define as the business of dealing in money and the instruments of credit. Originally bankers were simply dealers in money; but with the growth of credit to its present enormous and complex dimensions, the part played by the precious metals has acquired but minor importance. Bankers now chiefly deal in credit and the various instruments of credit, and these promises to pay gold on demand or at fixed periods are usually liquidated without the use of gold or silver. Indeed, it would be impossible at any given time to perform all the existing promises, and our system is based on mutual confidence and forbearance. When through various causes a temporary lapse of confidence occurs, and an unusual demand for gold ensues, we get what is called a commercial crisis or panic, often causing great distress, and endangering our whole business system.

The smallness of the part played by coin in our banking transactions can be seen by the following table, prepared by Sir John Lubbock, and published in the *Statistical Journal*, of the business transactions of Robarts, Lubbock, and Company, in the year 1864. Of the twenty-three millions which passed through their hands, the particulars are as follows:—

	Per cent.
Cheques and bills passed through the Clearing House	70·8
Cheques and bills collected otherwise	23·3
Bank of England notes	5·0
Coin	·6
Country bank notes	·3
	100·0

Again, Mr. R. H. Inglis Palgrave, writing in the same journal of the Manchester and Salford Bank, says that coin and notes formed 53 per cent of the total transactions in 1859, 42 per cent in 1864, and 32 per cent in 1872 and of this latter percentage in 1872 only 5 per cent was coin.

The most important function of a banker, then, is his dealings in the instruments of credit, cheques, bills of exchange, and notes. A cheque is a bill of exchange drawn on demand upon a banker, and a bill of exchange is further defined by the Bills of Exchange Act of 1882 as "an unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the persons to whom it is addressed to pay on demand, or at a fixed or determinable future time, a sum certain in money to or to the order of a specified person, or to bearer."

Clearing House.—The business of collecting cheques forms the major part of a banker's duties, and is chiefly carried out through the London Clearing House. This latter institution was in its origin a voluntary association of certain London private bankers founded about the year 1775 for the purpose of exchanging cheques drawn upon each other. It was not till 1854 that joint-stock banks were admitted to the privileges of the Clearing House. This extension was, however, followed in 1858 by the establishment of the Country Clearing, by means of which country banks were enabled to collect the cheques drawn upon each other without the expense and trouble of presenting them direct through the post. Every country bank of any importance now has a London agent with a seat at the Clearing House, through which he collects the cheques he receives in the course of his business. The number of clearing bankers is now 18, and they are as follows:—

Barclay and Co., Ltd.
Capital and Counties Bank, Ltd.
Glyn, Mills, Currie, and Co.
Lloyds Bank, Ltd.
London and County Bank, Ltd.
London Joint Stock Bank, Ltd.
London City and Midland Bank, Ltd.
London and South-Western Bank, Ltd.
London and Westminster Bank, Ltd.
Martin's Bank, Ltd.
Metropolitan Bank of England and Wales, Ltd.
National Bank, Ltd.
National Provincial Bank of England, Ltd.
Parr's Bank, Ltd.
Prescott, Dimsdale, Cave, Tugwell, and Co., Ltd.
Robarts, Lubbock, and Co.
The Union of London and Smith's Bank, Ltd.
Williams Deacon's Bank, Ltd.

Besides these the Bank of England clears on one side only—that is to say, it collects the cheques which it receives from its customers through the Clearing House, but requires other banks to present cheques drawn upon it at the Bank of England.

Every clearing bank sends a certain number of clerks to the House in Post Office Court, Lombard Street, with bundles of cheques, technically known as "charges," drawn upon the other members of the House, or upon banks for which they are agents, and receives in return bundles of cheques drawn upon himself or his country correspondents. There are three clearings during the day, the Morning Clearing, the Country Clearing, and the Afternoon Clearing. The balances are settled by drafts upon the Bank of England, where every clearing banker keeps an account. The Bank of England transfers these balances from the account of one bank to that of the others, and thus the whole clearing is effected without the use of coin or notes. All "returns"—that is to say, cheques which are not paid owing either to some technical error in the cheque or through want of funds—must be received back at the Clearing House the same day in the case of London banks, and by the morning of the third day in the case of country banks. Country banks do not, however, send unpaids back to the Clearing House, but return them direct to the bank whose crossing they bear and advise the House of the fact. The total amounts of the cheques passed through

the London Clearing House reach enormous dimensions, as the following figures show:—

Year.	Total Amounts of Clearings.
1870	£3,914,220,000
1880	5,794,238,000
1890	7,801,048,000
1898	8,097,291,000
1899	9,150,269,000
1900	8,960,170,000

But these figures do not represent all the cheques and bills collected by bankers. A large proportion of the cheques drawn upon the suburban branches of the large English banks are presented direct by "walk clerks," while there are provincial clearing houses at Birmingham, Bristol, Leeds, Leicester, Liverpool, Manchester, and Newcastle-on-Tyne, where the local banks clear the cheques drawn upon each other. Scotland possesses clearing houses in Edinburgh and Glasgow, and in Ireland there is one in Dublin.

There is, however, no international clearing house between the three kingdoms. Although most of the Scotch banks have branches in London, they have been refused admittance to the London Clearing House, and cheques which are circulated in a country other than that in which the bank is situated are usually collected direct through the post. Thus, if an English country banker acquires a cheque on a Scotch bank, he sends it direct and usually receives in return a draft on London.

Some of the larger banks in each country have made mutual arrangements with each other to clear one another's cheques, but these are merely private arrangements, and some system of international clearing between the three countries is badly needed. Under the present arrangement it is usual in the international collection to make a charge varying from 1s. to 2s. 6d. per £100.

Cheques.—Having seen how a banker collects cheques which come into his hands, we must now consider what are the requisites of a valid cheque, and what are the rights and responsibilities of those parties through whose hands it passes. Cheques are usually drawn upon the printed forms supplied by the banks, but they may be drawn upon plain paper, though this is a practice which is strongly discouraged by bankers, as the difficulty of obtaining a printed cheque is a great obstacle to a would-be forger. All cheques drawn, payable, or negotiated in the United Kingdom must bear a stamp of the value of one penny, either impressed or adhesive, with the exception of certain cheques drawn upon Government account, or by registered friendly societies, or by one bank upon another for the purpose of settling a clearing between the two banks. A receipt on a stamped cheque formerly did not require an additional stamp, but this was altered by the Finance Act of 1895, and all such receipts must now be stamped.

By section 18, clause 2, of the Bills of Exchange Act, a cheque "is not invalid by reason that it is ante-dated, or post-dated, or that it bears date on a Sunday." But although a post-dated cheque is valid under the terms of this Act, the practice is apparently a contravention of the Stamp Act, though the question has never been legally settled. A banker may not debit his customer's account with a post-dated cheque, but must hold it until it becomes due; if he pays the money for the cheque before the due date, he of course runs the risk that the customer may have no funds left by the time he is legally entitled to debit the account. All cheques are drawn payable "to order" or "to bearer"; if neither is mentioned on the

cheque it is assumed that it is payable to order. All cheques except those payable to "bearer" require the endorsement of the payee, and the incorrect endorsement of a cheque is a matter which causes a great deal of trouble and loss of time to bankers. The name of the endorser must be spelled in the same way as that of the payee, and should the latter be incorrect the endorser should write it as spelled, adding the correct name beneath for identification.

All titles or marks of rank should be omitted as prefixes of the endorsement, but may be added as descriptions. Thus "Mr. Smith" is incorrect as an endorsement of a cheque payable to "Mr. Smith," but "Col. Jones" may be endorsed "W. Jones, Col." It is often difficult to state whether any particular form of endorsement is correct or not, because there may have been no legal decision on the point, but in case such an endorsement came before a court of law the custom of bankers would probably have the greatest effect in settling the question, so that it is fairly safe to accept the ruling usually given by a banker in such cases. It is not considered necessary to sign the full Christian names in an endorsement; so long as the initials agree with those in the body of the cheque it is sufficient. If a cheque is payable to "Mrs. John Jones," it should be endorsed by the lady's own name, with the addition "wife of John Jones" or "widow of John Jones," as the case may be. In the case of a trading firm or company the matter is more complex: if the style of the firm consists of the names of the partners, as for instance "Brown and Evans" or "John Smith and Sons," any of the partners may write the name of the firm, and by so doing he binds his copartners: but in some cases an agent may have to endorse; if so, he may sign *per procuration*, thus—

per pro Brown and Evans,
HENRY HARRIS.

A per procuration endorsement is valid in the case of an individual, a private firm, or a limited company. Of course an agent must be authorised by his principal to sign "per pro," but a banker is not bound to inquire as to the possession of this authority in an endorsement on a cheque; and although the principal is not bound by the unauthorised signature, the banker is exempt from liability in paying the cheque. Until recently bankers refused to pay on the endorsement of a limited liability company by procuration unless the official capacity of the agent was added, but this form of endorsement is now generally accepted.

An agent may also endorse by signing "for" or "on behalf of" his principals with the addition of his official designation, thus—

For the Middlesex Gas Company,
JAMES ROBINSON,
Secretary.

A banker accepts the signature in an endorsement of such officials as customarily have the power to sign for a company; thus the secretary, manager, director, or cashier may sign officially, but the description "clerk" or "foreman" would usually be refused. An agent cannot sign "for" or "on behalf of" without adding his official capacity, and in the case of an individual this form of endorsement must not be used. "For John Jones, Henry Smith" is incorrect; in such cases a per procuration form of endorsement must be used unless the agent holds a power of attorney, when he may sign

John Jones,
By his attorney, HENRY SMITH.

One of the most usual instances of incorrect endorsement is when the cheque is made payable to "Messrs. Smith," or "Messrs. Robinson." This literally means a firm all of whose members are named Smith or Robinson; it is, in fact, simply the plural of Mr. Smith. "Smith and Co." is therefore not the correct method of endorsing such cheques. The proper form is "J. and S. Smith," or "Smith and Son," or "Smith Bros," or even simply "Smiths," though many banks refuse to recognise this last form of signature. It is a legal maxim that an agent has no power to delegate his authority, therefore an endorsement in the form—

For the Middlesex Gas Co., Limited,
per pro J. Jones, Manager,
HENRY SMITH,

is incorrect; in the same way

For the Middlesex Gas Co., Limited,
J. JONES, *pro* Manager,

is wrong, though many banks endorse cheques payable to them in this manner. If a cheque is payable to "the executors of Henry James," it is usual for one executor to sign for the rest in the following form:—

For self and co-executors of Henry James,
JOHN SMITH.

On the other hand, trustees must all sign in an endorsement.

Should the payee of a cheque be unable to write, he should make his mark in the presence of a witness. The following is the usual form:—

Henry Jones
X
his mark.
Witness, J. SMITH,
10 West St., London, N.

The witness must in all such cases add his address.

An endorsement may be either "in blank" or "special." An endorsement in blank specifies no payee; a special endorsement specifies the person to whom or to whose order the bill is to be payable, thus—

Pay to the order of John Jones,
HENRY SMITH.

Although a cheque be endorsed in blank, any subsequent holder may specially endorse it to a further endorsee, and the cheque will then require this last endorsee's signature before payment.

All endorsers of a cheque by so doing guarantee the genuineness of it, and if the cheque is unpaid the holder can compel a previous endorser to refund the money, provided he has been served with due notice of dishonour, as we shall see later on.

It is usual to write the amount of a cheque in both words and figures, though the latter are not legally necessary. A banker, however, always requires the amount to be written in words. Should the two statements of the amount differ from one another, a banker may treat the one in words as the correct one, but in practice he will return the cheque unpaid with the answer "body and figures differ" or "amounts differ."

If the date be correct, the amounts agree, and the endorsement be correct, the banker will in most cases be able to pay the cheque; should

there be, however, insufficient money to the credit of the drawer, and the banker be unwilling to allow his customer to overdraw his account, the cheque will usually be returned with the answer "Refer to drawer" or "R/D"; other banks prefer the forms "n/s" or "not sufficient," or "n. p. f.," "not provided for." In England a banker must write the answer on a cheque drawn upon him which he returns unpaid; in Scotland and Ireland, however, such is not always customary, and if a cheque is returned without an answer, it is presumed that the drawer has not sufficient funds. If a cheque is torn quite in two a banker will refuse to pay it, returning it with the answer "mutilated cheque"; but if the tear does not extend right across the document, so that it is still in one piece, it will usually be paid. In the former case the holder must obtain a fresh cheque from the drawer, unless he can give his banker satisfactory evidence that the mutilation was accidental, in which case the collecting banker may indemnify the paying banker against possible loss. If the drawer of a cheque die, a banker must not pay any of his cheques after he has received notice of death; the holder of the cheque will then inform the executors of the deceased of his claim against the estate.

The drawer of a cheque may order his banker not to pay any particular cheque upon presentation, or, as it is usually called, "stop payment" of a cheque. But we must be careful to note that the drawer does not by doing so rid himself of his responsibility for the amount of the cheque. He cannot stop payment of a cheque as against a "*bona fide* holder for value." A *bona fide* holder for value or "holder in due course" is defined by the Bills of Exchange Act, 1882, 29 (1), as "A holder who has taken a bill, complete and regular on the face of it, under the following conditions, namely—

"(*a*) That he became the holder of it before it was overdue, and without notice that it had been previously dishonoured, if such was the fact.

"(*b*) That he took the bill in good faith and for value, and that at the time the bill was negotiated to him he had no notice of any defect in the title of the person who negotiated it."

The holder in due course cannot compel the banker to pay the cheque; he has no recourse against the latter, who is responsible only to his customer, but he can sue the drawer of the cheque and compel him to pay the amount. "He holds the bill free from any defect of title of prior parties, as well as from mere personal defences available to prior parties among themselves, and may enforce payment against all parties liable on the bill" (Bills of Exchange Act, 38, 2).

It is necessary to note, however, that by section 24 of this Act no one can acquire a valid title to a bill or cheque through a forged endorsement. If, then, a man holds a cheque on which a previous endorsement has been forged, he does not become a "holder in due course," and cannot enforce payment.

There is one description of cheque to which we have not yet referred, and which is very little understood by the general public: this is the "crossed cheque." The effect of crossing a cheque, that is to say, of placing two parallel lines across its face, with or without the words "and company" enclosed, is that the banker on whom it is drawn must not pay it in cash across his counter, but only to another bank. The crossing of a cheque may not be on the back, and it may be added by the drawer or by any holder. A cheque may be crossed generally or specially, that is to say, with the name of a banker added, in which case the banker on whom it is drawn must pay

it only to the bank with whose name it is crossed. Section 79 of the Bills of Exchange Act defines the duties and responsibilities of a banker in dealing with a crossed cheque. Subsection (1) says: "When a cheque is crossed specially to more than one banker, except when crossed to an agent for collection, being a banker, the bank on whom it is drawn shall refuse payment thereof.

"(2) When the banker on whom a cheque is drawn which is so crossed nevertheless pays the same, or pays a cheque crossed generally otherwise than to a banker, or if crossed specially otherwise than to the banker to whom it is crossed, or his agent for collection being a banker, he is liable to the true owner of the cheque for any loss he may sustain owing to the cheque having been so paid."

Many people cross a cheque generally before sending it through the post, with a vague idea that it ensures the money being paid to none but the true owner; but of course this is a mistaken notion. If the cheque is stolen, or gets into dishonest hands, the thief cannot present it for payment across the counter of the bank on which it is drawn, and to this extent he is hindered in realising the amount; but should the cheque be payable to bearer, or be duly endorsed, and it gets into the hands of a third person, who takes it for value and in good faith, this latter person becomes a holder in due course, and can sue the drawer for the amount. To ensure, as far as possible, a cheque getting into the hands of none but the true owner, and of rendering it worthless to any one else, it should have the words "not negotiable" added to the crossing. The quality of negotiability is one which distinguishes coin, bills of exchange, cheques, and certain other documents from other forms of property. The qualities of a negotiable instrument are three: (1) Every person who acquires a negotiable instrument in good faith and for value shall (unless he gets it through a forged endorsement) have a good title to it, notwithstanding the possible defects of any previous holder. This is in direct opposition to the common law dictum, that no one can transfer a better title than he himself possesses. (2) The holder of a negotiable instrument can sue on it in his own name. (3) In the absence of proof to the contrary, it is assumed that valuable consideration was given for it. The mere crossing of a cheque does not deprive it of its negotiability; it only restricts this quality in certain cases, but the addition of the words "not negotiable" brings it within the scope of the common law, and every one who gives value for such a cheque does so at his peril; he takes it subject to any defects in the title of a previous holder, and if the cheque has been affected by fraud he cannot enforce it against the drawer or any holder previous to the fraud. As the crossing of a cheque necessitates its collection by a banker, and since, under the common law, if a banker collects a cheque for any one who is not the true owner he can be sued for "wrongful conversion," it was thought necessary to add a clause giving some measure of protection to bankers. Section 82 of the Bills of Exchange Act (which reproduces section 12 of the Crossed Cheque Act, 1876) says: "When a banker in good faith and without negligence receives payment for a customer of a cheque crossed generally or specially to himself, and the customer has no title, or a defective title thereto, the banker shall not incur any liability to the true owner of the cheque by reason only of having received such payment." The protection afforded to bankers by this clause reaches only to crossed cheques, and the law remains unchanged in the case of open cheques; and it was decided in *Bissell* v. *Fox* in 1884 that a banker cannot obtain protection by crossing cheques after they have reached his hands. The question of the liability of a collecting banker

is one of the most complex and least satisfactory of the problems he has to face. A case which throws considerable light on the subject was decided in the House of Lords on 23rd July 1901—*Great Western Railway* v. *London and County Bank*. Huggins, a collector of the plaintiffs, obtained from them by fraud a crossed cheque marked "not negotiable," drawn to his order on the London Joint Stock Bank. Huggins was well known to the Wantage branch of the defendant bank, where he had cashed cheques for many years, though he had no account. In this case part of the money was paid in to another account at the branch, and the rest handed to him in cash, with which he decamped. The drawers of the cheque sued the bank for the money, contending that the latter had negotiated a cheque marked "not negotiable," and that they had therefore acquired no title through Huggins. The bank pleaded section 82 of the Bills of Exchange Act, that they had collected the cheque for a customer. They argued that, although a stranger who came to a bank upon an isolated occasion to obtain money for a cheque may not be a "customer," yet it had been held in *Matthews* v. *Brown* that the term customer involved "use and habit," and that Huggins could fairly be claimed as such. Judgment was given for the plaintiffs, on the grounds that Huggins was not a customer, and that as the bank parted with the money before the cheque was presented, they had not collected it for Huggins but for themselves.

This last ruling is one of the greatest importance to bankers, and it seems to deprive them of the greater part of the protection given them by section 82. It is the universal practice of bankers to credit their customers at once with cheques drawn upon banks in the same town, and in most cases with cheques drawn upon London banks. In these cases it seems, in the light of the above ruling, and also of a similar one in *Bissell* v. *Fox* in 1884, that the bank collects the cheques for themselves and not for their customers, and that the transaction falls outside the scope of the above section of the Bills of Exchange Act.

A custom has grown up recently for the drawer or holder of a cheque crossed generally or specially to add the words "For account of payee only," or "Account of John Jones." This practice has received no statutory sanction, and its operation is doubtful. As far as the paying banker is concerned, it would seem that he is free from liability, for he has no means of knowing whether the cheque has been credited as directed or no. As regards the collecting banker, however, such words seem to be a direction to him to deal with the cheque in a certain way, and if he disregarded the direction, it is very probable that he would be held liable in damages. The only case dealing with the point is *National Bank* v. *Silke*, 1890, and in this case the defendants contended that the addition of such words restricted the transferability of the cheque.

A customer of the National Bank, named Moriarty, paid in to his account a cheque drawn by the defendant Silke, and crossed "Account of J. F. Moriarty, Esq., National Bank, Dublin." The bank allowed Moriarty to draw against this cheque before it was cleared, and when it was returned unpaid with the answer, "Order not to pay," the bank sued the drawer as holders for value. Silke concluded, however, that the crossing in the manner recorded above had the effect of restricting the transferability of the cheque under section 8, subsection 4, of the Bills of Exchange Act, which says: "A bill is payable to order which is expressed to be so payable, or which is expressed to be payable to a certain person, and does not contain words prohibiting transfer or indicating an intention that it should not be transferable." The defendant therefore claimed that the

National Bank were not the holders for value, and could acquire no title to a cheque which was in effect not transferable.

The Court, however, decided against this contention, and gave judgment for the bank, which was upheld by the Court of Appeal.

Bills of Exchange.—To turn now to the subject of bills of exchange other than cheques. A bill of exchange requires acceptance in writing by the drawee or person on whom it is drawn before the latter incurs any liability. The acceptance of a bill is the signification by the drawee of his assent to the order of the drawer. It must be written on the bill and be signed by the drawee. An acceptance may be either general, which is the usual form, or it may be conditional or partial; but in presenting a bill for acceptance, a partial or conditional acceptance would usually be refused in the absence of instructions to the contrary. The usual form of acceptance is to write across the face of the bill, "Accepted payable at . . . (naming an address, usually that of a banker), John Jones." If no address is mentioned in the acceptance, the bill is payable at the address of the drawee mentioned on the bill.

The usual form for drawing a bill of exchange is as follows:—

LONDON,.....

Three months after date pay to the order of John Smith the sum of one hundred pounds for value received. HENRY JAMES.

To Mr. Edward Turner,
180 West Street, Birmingham.

A bill may be drawn in a "set" of two or three parts, "each part of the set being numbered, and containing a reference to the other parts, the whole of the parts constituting one bill" (Bills of Exchange Act, sec. 71). In this case the bill should be drawn:—"Three months after date pay this $\left.\begin{matrix}\text{first}\\\text{second}\end{matrix}\right\}$ of exchange $\left(\begin{matrix}\text{second}\\\text{first}\end{matrix}\right.\}$ of the same tenor and date being unpaid), to the order of," etc. The place from which the bill is dated should always be mentioned, otherwise it may not be possible to tell whether it is an inland or a foreign bill. A bill may be drawn on demand, or at sight, or on presentation, or so many days after sight, or on such and such a date, or so many days or months after date. When a bill is not payable on demand, or on sight or presentation, three days, called days of grace, must be added to the time of payment as fixed by the bill, and the bill is payable on the last day of grace. Should this due day fall on a Sunday, Christmas Day, Good Friday, or day appointed by royal proclamation as a public fast or thanksgiving day, it is payable on the preceding business day. Should it, however, fall due on a Bank Holiday, or when the last day of grace is a Sunday and the second day of grace a Bank Holiday, it is payable on the succeeding business day. Bills drawn by the Bank of England upon themselves do not take three days' grace. A bill drawn at one month after date, and dated 31st January, is due 3rd March, and a bill dated 30th June, drawn at one month after date, is due 2nd August, the term month meaning always calendar month. A bill drawn "after sight" is reckoned from the day on which it is presented for acceptance, and the acceptor should always write the date of his acceptance on the bill. If a bill is drawn in the form—"On 1st October *fixed*," it does not take the three days' grace.

The stamp on a bill of exchange drawn on demand, or at sight or on presentation, or at three days or less after sight, is one penny, which may be denoted by an adhesive or an impressed stamp. The stamp to be used

is an inland revenue stamp, whether the bill of exchange is inland or foreign. The stamps on bills of exchange drawn after date, or at more than three days' sight, if they are negotiated, drawn, or payable in the United Kingdom, are as follows:—

When the amount of the bill does not exceed £5	1d.
Exceeds £5 and does not exceed £10	2d.
„ £10 „ £25	3d.
„ £25 „ £50	6d.
„ £50 „ £75	9d.
„ £75 „ £100	1s.
For every £100 and every fractional part of £100	1s.

If a bill drawn payable abroad is afterwards paid or negotiated in the United Kingdom, the scale of stamping is, under the terms of the Finance Act of 1899, less than the above; viz. exceeding £50 but not exceeding £100, 6d.; for every succeeding £100 or part of £100, 6d. For bills under £50 the rate is the same as for inland bills.

The *ad valorem* stamps on bills drawn out of the United Kingdom are to be denoted by adhesive foreign bill stamps; in other cases the stamp must be an impressed inland bill stamp. It is most necessary when drawing a bill to take care that it is drawn upon paper stamped to the correct amount; if the amount of the impressed stamp is insufficient, not only will a banker refuse to pay it, but it would be impossible to maintain any suit on the bill in a court of law.

An inland bill must be drawn on paper already stamped. The only occasion when it can be stamped afterwards is when the bill has been drawn upon paper bearing an impressed stamp of sufficient amount but of improper denomination; in this case it can be restamped on payment of a penalty varying from 40s. to £10. Where a bill is drawn in a set it is only necessary to stamp one of the set.

All adhesive stamps on bills of exchange or cheques must be cancelled by the person affixing his name before the document leaves his hands, "by writing on or across the stamp his name or initials, or the name or initials of his firm, together with the true date of his so writing, or otherwise effectively cancelling the stamp." The fine for neglect of this precaution is £10.

This is a clause which is constantly neglected, and especially in the case of the penny stamp on a cheque drawn on blank paper; but not only should drawers remember that they are liable for a penalty under the Stamp Act, but the holders of such cheques are unable to sue as holders under the Bills of Exchange Act if the neglect to cancel the stamp can be proved. This was settled in the case of *Hobbs* v. *Cathie*. Cathie drew a cheque in favour of one Bull on plain paper and omitted to stamp it. Bull negotiated the cheque to the plaintiff, and before doing so stamped the cheque but omitted to cancel the stamp. Cathie stopped payment of the cheque, and Hobbs sued him as a holder for value. The judgment was in favour of the defendant on the grounds that the Act only permitted the use of an adhesive stamp on cheques on the condition that it was cancelled by the drawer or by the banker on whom the cheque was drawn; that in the present case the stamp was cancelled by neither the drawer nor the banker, and that it was therefore never duly stamped.

The law of endorsements on bills of exchange is, with one important exception, the same as that in the case of bankers' cheques which we have just discussed. An endorsement must be written on the bill, and although

it is usual to endorse on the back of the bill, an endorsement on the face is quite legal. When there is not room on the bill for all the endorsements, it is usual to attach a slip of paper called an "allonge"; and in order to avoid the possibility of fraud, it is better to write the last endorsement of the bill proper, partly on the "allonge" and partly on the bill.

The important difference between the endorsement of a bill of exchange and that of a cheque is that in the case of the latter, if "the banker on whom it is drawn pays the bill (*i.e.* cheque) in good faith and in the ordinary course of business, it is not incumbent on the banker to show that the endorsement of the payee, or any subsequent endorsement, was made by or under the authority of the person whose endorsement it purports to be, and the banker is deemed to have paid the bill in due course, although such endorsement has been forged or made without authority" (Bills of Exchange Act, 1882, sec. 60).

This protection to the banker against paying on a forged endorsement does not extend to bills of exchange, and as the banker in such cases is not acquainted with the signatures on the back of a bill presented for payment to him, he incurs considerable risk against which he can take no precaution.

The only protection afforded him is by sec. 7 (3) of the Act, which says: "Where the payee is a fictitious or non-existing person, the bill may be treated as payable to bearer."

This is the subsection on which was decided the well-known case of *Vagliano Brothers* v. *The Bank of England*. The plaintiffs were in the habit of accepting a large number of bills drawn on them from abroad, of which they advised the Bank of England, where the bills were payable, before the time when they fell due. Glyka, a confidential clerk of the plaintiffs, forged forty-three bills purporting to be drawn by Vucina, an Odessa merchant, to the order of C. Petridi and Company of Constantinople. Both of these were existing firms known to Vagliano Brothers, and Glyka having forged both the drawer's and endorser's signatures, induced the drawees to accept them. They were duly advised to the Bank of England by Vagliano Brothers with a request that they should be paid, and accordingly several of them were paid in cash across the counter to Glyka. When the fraud was discovered, Vagliano Brothers sued the Bank of England for the amount, £71,500, on the ground that the bank had paid the bills on a forged endorsement. The bank, on the other hand, contended that the action of the acceptors in advising payment of the bills justified them in so doing, and that the payees must under the circumstances be considered as "fictitious or non-existing persons" within the meaning of sec. 7 of the Bills of Exchange Act as quoted above.

The case was decided in the first instance in favour of Vagliano Brothers, and this was upheld by the Court of Appeal, but the House of Lords reversed the decision by a majority of six to two. As regards the forgery of the drawer's name, the acceptor is by sec. 54 of the Act precluded from denying the existence of the drawer, the genuineness of his signature, and his capacity and authority to draw the bill. Lord Macnaghton laid down that the proper meaning of a "fictitious" payee is "feigned or counterfeit," and that C. Petridi and Company were none the less fictitious persons because there were in existence real persons for whom these names were intended to pass muster.

If a bill is payable after sight, presentment for acceptance is necessary in order to fix the maturity of the bill. Any other bill which is drawn

payable elsewhere than at the residence or place of business of the drawer must be presented for acceptance before it can be presented for payment.

The holder of a bill payable after sight must either negotiate it or present it within a reasonable time; if not, the drawer and all previous endorsers are discharged from all liability on the bill. The question of what is a reasonable time is dependent upon the nature of the bill, the usage of the trade with respect to similar bills, and the facts of the case. Presentment for acceptance must be made at a reasonable hour on a business day to the drawee or some person authorised to accept or refuse acceptance on his behalf. Thus presentment to a clerk in the office of a business man is a proper presentment, but presentment to a servant at a private residence is not. Presentment through the post is sanctioned by custom, and is reckoned a legal presentment. If acceptance is refused the bill may be treated as dishonoured, and an immediate right of recourse against the drawer and all previous endorsers ensues.

All bills not payable on demand must be presented for payment on the day they fall due; bills payable on demand, or at sight or on presentation, must be presented for payment within a reasonable time.

The consequence of an omission to do this is that the drawer and all endorsers are released from liability on the bill, but not the acceptor. As a rule, bills are accepted payable at a banker's; they must accordingly be presented for payment as indicated in the acceptance. If no place of payment is mentioned, they must be presented for payment at the address of the acceptor as given in the bill. If an acceptor has changed his address since the time he accepted the bill, he must either make arrangments that it shall be paid at the original address, or if he can trace the bill, he should notify the holder of his change of address, otherwise there will be a risk of the bill being dishonoured. If a bill is drawn in a set, the drawee must be careful to accept one part only, or he will be separately liable on each part accepted.

When a bill is dishonoured by non-acceptance or non-payment, notice of dishonour must be given to the drawer and each endorser, or else they are released from liability on the bill. If the party to whom notice is to be sent is resident within the same town, it must reach him on the day following the dishonour of the bill; if otherwise, notice must be sent on the day following the dishonour. Thus it must not be forgotten that if a bill is "domiciled" or made payable at a banker's, he has the right to keep it a day after maturity before sending it back unpaid, if the holder does not live in the same town.

A banker usually gives notice of dishonour by the simple return of the bill with the answer written upon it. The usual answers in this case are "R/A" or "refer to acceptor," "n/a" or "no advice," or "n/o" or "no orders." If the man who receives back a bill from his bankers wishes to keep his recourse against a previous endorser or the drawer, he is allowed the same time to serve notice of dishonour, namely, it must reach the party by the next day if he lives in the same town, if not he must forward the notice by the day following the one he received it. This applies to cheques received back unpaid, when notice must be sent to the drawer as well as to any endorser against whom recourse is required. All foreign bills which are dishonoured, whether by non-acceptance or non-payment, require to be protested; if a bill has been protested for non-acceptance it is not legally necessary to protest it afterwards for non-payment, but this is often done in order to satisfy the requirements of the country in which the bill is drawn. In the case of an inland bill a protest is not necessary, but it is

often made at the request of the holder. All protests must be made on the day on which the bill is dishonoured, but it is sufficient if the bill is merely noted for protest on the day of dishonour, the noting may be extended to a formal protest at any time considered necessary; by this means part of the expense of a formal protest is saved. It is the practice of most bankers to note all bills, whether foreign or inland, unless they have received instructions to the contrary from the holder of the bill. The protest must be made at the place where the bill is dishonoured, except when a bill is presented and returned through the post, when it may be protested at the place to which it is returned, but this latter practice is local and unusual. It may happen that there is no notary in a town where a bill is dishonoured; in this case a householder's protest should be drawn up in the presence of two witnesses and stamped as follows: where the duty on the bill does not exceed 1s., the same duty as the bill or note; in other cases 1s. Postage stamps may be used. For the convenience of any who may have to draw up a householder's protest, we give below the form suggested in the 1st Schedule to the Bills of Exchange Act, 1882.

Form of Protest which may be used when the services of a Notary are not obtainable.

Know all men that I, A. B. (householder), of in the county of in the United Kingdom, at the request of C. D., there being no notary public available, did on the day of 19 , at , demand payment (or acceptance) of the bill of exchange hereunder written, from E. F., to which demand he made answer (state answer, if any), wherefore I now, in the presence of G. H. and J. K., do protest the said bill of exchange.

(Signed) A. B.
G. H. } *Witnesses.*
J. K. }

N.B.—The bill itself should be annexed, or a copy of the bill, and all that is written thereon should be underwritten.

When a bill has been noted or protested, and is afterwards presented again for payment, the notarial expenses should be demanded as well as the original amount of the bill, and a banker is authorised to debit his customer's account with such expenses without obtaining the direct permission of the acceptor.

An accommodation bill is a bill which has been accepted by a drawer without receiving value for the same, and for the purpose of lending his name to some other person. This latter person, as a rule, provides for the bill before maturity. The transaction is a method of borrowing money, the holder discounting the bill at his banker's and withdrawing it before presentment.

When an alteration in a material part of a bill of exchange is made, that is to say, in the date, amount payable, the time of payment, and the place of payment, the alteration should be initialed by both drawer and acceptor. The acceptor of a bill is not, however, bound to see that it is drawn in such a manner as to prevent the fraudulent alteration of the bill. Of course it is to the interests of all the honest parties to a bill that such precautions should be taken, and it is advisable to see that a bill is not drawn on paper bearing a larger stamp than necessary, and that no blank spaces are left in the document. But no legal obligation to do this exists, as has been held in the case of *Scholfield* v. *The Earl of Londesborough*. A man named Sanders drew a bill for £500 upon the defendant, the Earl of Londesborough. It was drawn upon a £2 stamp, which was sufficient to cover an amount up to £4000. The amount of the bill was written in

figures, with sufficient space between the £ and the 5 to admit of the insertion of another figure. The body of the bill ran: "Pay to me or my order the sum of," then a blank space; on the next line were the words "five hundred pounds," etc. The man Sanders obtained the defendant's acceptance to the bill in the usual course, and then fraudulently altered the amount to £3500. The bill in this form was negotiated, and came into the hands of the plaintiff in good faith and for valuable consideration. The bill was not paid, and Scholfield sued the acceptor for the full amount, on the ground that he was "estopped" from pleading the forgery by reason of negligence in accepting the bill in the form it was drawn. The Court of Appeal decided in favour of the defendant, and the Master of the Rolls stated the opinion that the acceptor had no duty towards the drawer or endorser of a bill of exchange except that of paying it when presented.

Promissory Notes.—A promissory note is "an unconditional promise in writing made by one person to another, signed by the maker, engaging to pay, on demand or at a fixed or determinable future time, a sum certain in money to or to the order of a specified person or to bearer" (Bills of Exchange Act). The following is the usual form in which a promissory note is drawn up:—

LONDON,.....

One month after date $\frac{\text{I}}{\text{we}}$ promise (or we jointly and severally promise) to pay to the order of the sum of for value received.

(Signed) HENRY JONES.

The "maker" of a promissory note stands in the same position towards the endorsers or holders as the acceptor of a bill of exchange, and if we except the provisions relating to acceptance, the law is the same for the two classes of documents; a promissory note does not require accepting by the maker. Promissory notes are not drawn in a set, nor is protest legally necessary in the case of the dishonour of a foreign note. The stamp duties are the same for the two classes of documents, except in the case of bankers' promissory notes to bearer on demand, which are stamped at a higher rate and can be reissued. The issue of these is, as we have seen, controlled by the Bank Charter Acts of 1844-45.

Banker and Customer.—We come now to consider the relations between a banker and his customer in the working of a banking account. A banker impliedly contracts to pay his customer's cheques while there is sufficient money remaining to the credit of the customer, in return for the advantages he derives from the use of his customer's capital, or else for the receipt of a certain sum in commission. In the event of a breach of contract the banker is liable to be mulcted in damages. This is the broad relationship between the two. The first formality to be undergone before opening an account at a bank is the production of a satisfactory introduction. If the account is transferred from another bank a banker's introduction is usually given, but in default of this the banker will accept the introduction of any respectable individual who is known to him. Of course it is advantageous to the customer to obtain as satisfactory an introducer as possible, as this may have some weight in determining the banker's answer to a request for temporary accommodation. The banker will then require the customer to write his name and signature and the particulars of his address and occupation in the signature book.

It is desirable to come to some understanding with the bank manager as to the terms on which the account is to be kept. The amount of the balance which a bank expects a customer to keep in order to avoid a charge

for the management of an account, varies according to the character of the account and the standing of the bank. Thus a business customer with a large turnover is required to keep a very much larger balance than a private individual who only uses his account for his household and personal expenses. Again, a bank in the City of London would probably often make a charge for keeping an account which a small country branch would keep for nothing. Under these circumstances it is impossible to put into figures the probable requirements of a bank manager.

It is well to be as open as possible to a banker when making arrangements about opening an account. A man's financial reputation may lie in his banker's hands, and nothing induces caution in a banker's dealings with a customer so much as a show of reserve or secrecy on the latter's part. In many instances a banker has to refuse accommodation to a customer through lack of knowledge of his true position, when he would willingly have granted it, had a little more confidence been reposed in him.

Having satisfied the bank in the matter of introduction, and deposited the money wherewith the account is to be opened, a cheque-book will be issued to him, if the introduction is sufficiently good to warrant it being done at once, but in many cases the banker will require the cheques deposited to be cleared before doing so.

It is usual for bankers to credit a customer immediately with cheques on banks in the same town, and in the case of most English banks, with cheques drawn on London banks. But in the case of cheques which have to be collected through the country clearing, or those drawn on a bank in one of the other countries of the United Kingdom, many bankers require their customers to wait until the cheques have been cleared before crediting their accounts with the proceeds. This usually occupies three, four, or five days.

In paying in cheques it is a frequent practice of customers to ask for part of the amount to be given them in money, and the rest to be credited to their account. Some banks refuse to do this, and it is a practice not to be encouraged: it is bad book-keeping, because the whole of the transaction does not show in the pass-book, and may lead to confusion when the account has to be checked. If the customer requires part of the amount in cash, the proper method is to credit his account with the total and get him to draw a cheque for what money he may require. In drawing cheques the drawer is bound to take reasonable precautions against a possible fraudulent alteration, or he may be held to have contributed to the subsequent fraud by his negligence, and be estopped from setting up the bank's negligence in paying the cheque. In discussing the case of *Scholfield* v. *Londesborough*, we saw that the acceptor of a bill of exchange has no such onus thrown upon him; but in the same case Lord Shand expressed the opinion: "The case of *Young* v. *Grote*, between a banker and his customer, was one in which there was the relation of parties contracting with each other, . . . and this relation inferred, if not expressly, at least by implication, the duty and obligation on the customer's part, in issuing cheques on his banker to third parties, to take care that these were not in such a form as to give the means of enlarging their amount without this being readily detected."

The case of *Marcussen* v. *The Birkbeck Bank* in 1889 turned upon the same point. The plaintiff had drawn a cheque for £8:5s. in such a way that a fraudulent holder had altered it to £80:5s., by adding a cipher after the 8 in the figures and a "y" in the words. Judgment was given for the defendant bank on the ground of negligence; and Mr. Justice Matthew, in summing up, said that the law on the subject was that "if a cheque was so

carelessly drawn as to expose a banker, using reasonable care, to the risk of paying what was not intended, then the banker was not liable."

When paying in cheques or money to the credit of his own account, a customer does not usually ask for a receipt from his banker, but if he requires one the banker must give it. Such receipt is exempt from stamp duty so long as a third party's name does not occur in it. If it is desirable to have some proof that the cheques have been received by the banker, as, for instance, when they are entrusted to a messenger, it is usual to obtain from the banker a book of credit slips issued in duplicate. The banker then retains one part, and the cashier signs or initials the corresponding part and returns it to the customer.

Sometimes a customer pays in a cheque to his credit for a special purpose, as, for instance, in order to provide for a cheque which he has drawn. This is called "earmarking" a credit, and if a banker receives a credit for such a special purpose, he is bound so to apply it, and cannot use it as a means of reducing his customer's debt to him if the account should be overdrawn at the time.

A banker is bound to furnish his customer with a copy of his account if desired, and this is done by issuing a "pass-book," which is a copy of the banker's ledger. An entry in a pass-book is not conclusive proof of the truth of the entry, but if a customer can show that he has suffered loss or damage through being misled by a false entry in a pass-book, he can obtain damages against the banker. In the same way acquiescence in certain entries in a pass-book on the part of a customer has been held to prevent him from afterwards denying the truth of such entries. Thus in *Chatterton* v. *London and County Banking Company, Limited*, 1890, the plaintiff sued the bank for the amount of twenty-five cheques which he alleged to be forgeries. On the bank's part it was stated that the signatures in question had been brought under the notice of the plaintiff, and he had stated them to be correct; moreover, he had each week ticked off the items in the pass-book with his own books, yet though the cheques alleged to be forged were entered in the pass-book, he failed to discover the fraud until the auditor inspected his books. Judgment was given for the defendant bank, and the jury found that the plaintiff's conduct had contributed to the loss.

In some banks it is the custom to enter amounts in the pass-book immediately they are paid in, but other banks refuse to do this, and issue the pass-book made up only to the evening of the preceding business day.

We have seen that by section 82 of the Bills of Exchange Act a banker who receives payment for a customer of a *crossed* cheque is protected from the consequences if the customer had no title to the cheque, provided he does so without negligence and in good faith. The position of a banker who receives payment of an uncrossed cheque under similar circumstances is not so happy, and he can claim no protection under this section; moreover, it has been held in *Bissell* v. *Fox* that a banker cannot bring himself within the protection of the section by crossing the cheques after they have come into his possession. If the banker collects cheques of this description for a man who has no title, whether a customer or not, the banker is liable under certain circumstances for wrongful conversion. He will stand or fall according to the validity of the title which the customer has, and which he gives to the banker. Thus, as a bearer cheque is negotiated by delivery only, the banker would acquire a good title from his customer, and would not be liable to the true owner. If, however, the cheque was an open one, payable to order, and the customer for whom the banker collected it had forged the endorsement, or if an agent, had endorsed it without the authority

of his principal, he could give the collecting bank no title to it, and the true owner would have a remedy against the banker. The case of *Bissell* v. *Fox*, 1884-85, is of great interest in this respect.

Shakeshift, a commercial traveller in the employ of the plaintiffs, was in the habit of remitting to his principals weekly the cheques he received in the course of business. Instead of doing this he opened an account with the plaintiff bank, and paid in to his own credit seven cheques payable to his principals, and endorsed by him "per pro." Three of these cheques were crossed and four open. The plaintiffs brought an action to recover the amounts of all these cheques, and contended that in the case of the crossed cheques the defendant bank had been guilty of negligence. Judgment was given for the plaintiffs in the case of all but one cheque, which was drawn on the defendants themselves, in which case the defendant bank were entitled to be considered as the "paying" bank and not the collectors of the cheque, and to be protected by section 60 of the Act, which relieves a bank from responsibility when paying on a forged endorsement. It was laid down in this case that the provisions of section 82 of the Act only apply when a banker receives a cheque already crossed, and not when a banker crosses a cheque to himself after receiving it for collection. This opinion seems at variance with section 77 (6), which expressly states: "When an uncrossed cheque, or a cheque crossed generally, is sent to a banker for collection, he may cross it specially to himself." This section was inserted in the Act at the suggestion of the Institute of Bankers for the express purpose of protecting bankers who collected uncrossed cheques, and of bringing them within the provisions of section 82; but if we accept the opinion laid down in this case as final, it has failed in its purpose.

It was also laid down that, in the case of the crossed cheques, the bankers had not acted without negligence, in that, knowing Shakeshift was an agent they should have inquired as to his authority to endorse the cheques "per procuration" before passing them to the agent's own account. This is a decision of great importance to bankers, and devolves upon them the necessity for exercising great caution in dealing with the account of an agent; especially is this so when the agent and principal both keep their accounts at the same bank, and the bank are therefore unable to plead ignorance of the relationship between them. Bankers, when dealing with agents empowered by their customers to sign on their behalf, should see that the powers of the agent are sufficiently well defined in the written authority given by the principal. The power to draw cheques on behalf of a principal does not imply the power to overdraw the account, and such a power should be expressly mentioned in the authority delivered to the banker; otherwise the bank will probably be unable to claim against the principal for the amount of the overdraft. An agent cannot further delegate the power entrusted to him, and such power to act is terminated by the death, bankruptcy, or insanity of the principal.

In opening accounts in joint names, bankers require a written authority, signed by all, if cheques are to be drawn by one or part of their number. In the case of the decease of one of the number, the banker can pay the balance of the account to the survivors on proof of death, such proof usually being the exhibition of the burial certificate. If the banker possesses a written authority to honour the signature of each of the joint members, such a proof of death is unnecessary, as the survivors possess the power of dealing with the balance. In dealing with executorship accounts, the act of one executor or administrator is legally the act of all, and a banker is

justified in paying cheques drawn by a single executor without authority from the others; but it is advisable for a banker to obtain such a written authority, as although a single executor can bind the estate, he cannot bind the other executors personally. In transferring the balance of a deceased customer's account to that of his executor, a banker requires the probate of the will to be exhibited to him, or in case the deceased died intestate, a copy of the letters of administration. Then, upon satisfactory proof of the identity of the executors or administrators, the balance is transferred to an account usually opened in the executors' names as such.

Where the power to sign is given to a single executor, and this executor has also a private account with the same bank, the banker should be cautious in his dealings, or he may be held liable in case the executor misapplies the money of the estate to his own use. The law in such a case was laid down by Lord Cairns in the case of *Gray* v. *Johnston*: "In order to hold a banker justified in refusing to pay a demand of his customer (the customer being an executor, and drawing a cheque), there must, in the first place, be some misapplication, some breach of trust intended by the executor, and there must, in the second place, be proof that the bankers are privy to the intent to make this misapplication of the trust funds; and to that, I think, I may safely add, that if it be shown that any personal benefit to the bankers themselves is designed or stipulated for, that circumstance above all others will most readily establish the fact that the bankers are in privity with the breach of trust which is about to be committed."

As an example of what was meant, we will suppose a man to have a private overdrawn account, and also an executor account or trust account with a credit balance, on which he possessed the power to sign alone. The bankers press him for payment of his overdraft; he thereupon transfers a sum from his executor or trust account in satisfaction of it. If the executor defaulted, the bank would, in all probability, be compelled to refund to the estate the sum so transferred.

A trustee, unlike an executor, cannot by his own act bind his co-trustees. Whenever possible, a banker declines to open an account in the name of trustees as such, and prefers to treat it as an ordinary joint account; but should he feel compelled to recognise the trust character of the account, he should not accept an authority for one or more trustees to act for the whole body, as it is exceedingly doubtful whether he would be absolved from liability in case of the default of the acting trustee. If the affairs of a trustee come into a court of law, every protection possible is afforded to the trust funds by the court, and therefore a banker cannot be too wary in his dealings with them. If one of a body of trustees die, it should be inquired whether the deed of trust empowers the survivors to act, before giving them the power to do so; in the case of an executorship account, the power to act devolves naturally upon the survivors.

In business partnership accounts any partner can bind the firm by his own acts; moreover, any one who by word or deed leads others to believe that he is a partner, is liable on any contracts entered into upon the faith of such representations, and every partner is personally liable for all the obligations entered into by the firm.

If a partner retires from a firm which has an overdrawn account with a bank, he is not absolved from personal liability until the whole of the overdraft shall have been paid; but it must be noted in this connection that it is a legal maxim that the first item on the debit side of a current account is presumed to be discharged or reduced by the first item in priority of time on the credit side. If therefore in such a case it is desirable to

retain a claim upon the retiring partner, a new account should be opened when notice of the retirement is given to the bank.

In opening an account with a company registered under the Companies Acts, a banker usually requires a copy of a resolution passed by the directors, and signed by all or by the chairman, and countersigned by the secretary, authorising the banker to pay cheques signed in the manner the authority shall indicate.

If a company requires to overdraw its account or to borrow money, it is necessary for the banker to see a copy of the memorandum and articles of association of the company. By these documents the powers of the company are defined and controlled. It is not always expressly mentioned in a memorandum of association that a company has power to borrow money, but in the case of a trading company at all events this power is held to be implied, unless it is contrary to anything contained in the memorandum. If a company through its officers commits any act in excess of the powers so defined, it is held to be acting *ultra vires*, and the company is not bound by any such contract. A banker often has to assist in the floating of a new company, and he must remember that under the provisions of the Companies Acts of 1900 a company cannot enter into any contracts or borrow money until certain steps have been taken and a certificate has been issued by the Registrar of Public Companies, to the effect that the company is entitled to commence business. The issue of such a certificate is conclusive evidence that the necessary preliminaries have been properly carried out.

When a customer has satisfied his banker as to the manner cheques are to be drawn on the account, there is then a contract between them that the banker shall honour the cheques of the customer, if they are in order, so long as the customer has any money to his credit. In the event of the wrongful dishonour of the customer's cheques, he has a right to sue the banker for damages, but the holder of the cheque has no right against the banker, as there is no contract with him. He must have recourse against the drawer of the cheque, and any suit against the banker must be brought in the drawer's name.

A banker is not bound to pay his customer's cheques drawn against cheques in the course of collection which have not yet been credited, and even when a cheque is credited before it is cleared, it is the custom of many bankers, if it seem desirable to them, to return the customer's cheque unpaid with the answer, "Effects not cleared," if there is not sufficient money on the account exclusive of the uncleared cheque. Should a banker give a customer permission to overdraw his account to a certain extent for an agreed period, the banker must not dishonour his customer's cheques without notice before the expiration of such period, on the ground that circumstances have occurred causing him to reconsider his decision; but should a customer commit an act of bankruptcy, a banker is bound to refuse payment of his cheques whatever the state of his account, or he may be held liable to refund to the trustee in bankruptcy. It was decided by the Court, however, *In re* Walsh, 52 L.T. Rep. 694, that the mere calling together of a debtor's creditors and the offer to them of a composition is not an act of bankruptcy. No banker will knowingly open an account with an undischarged bankrupt, nor would it be safe for him to do so in the case of the wife of an undischarged bankrupt who was carrying on the husband's business.

The same obligation to refuse payment of a cheque exists when notice of the death of the drawer is received, or, in cases where the drawer signs

as agent, the death of the principal. If, however, an agent empowered to sign on his principal's account dies, and a cheque signed by him is presented after notice of death, a banker may yet pay the cheque.

In Scotland the holder of a cheque unpaid for want of funds acquires a lien on the balance of the account; if, therefore, a smaller cheque is afterwards presented, the banker must not pay it, although he has sufficient funds. This is not law in England, however.

It has been decided that a banker has no right to close a customer's account without giving him reasonable notice. In the case of *Buckingham* v. *The London and Midland Bank*, the plaintiff had a loan account secured by a mortgage on some houses and also a current account, with a balance standing to his credit. On entering the bank one day he was informed by the manager that the bank was dissatisfied with the value of the security, and that he must consider the account closed, the balance to his current account, amounting to £160, having been transferred in reduction of the loan account. The plaintiff informed the manager that certain bills accepted by him and domiciled with the bank fell due the next day, and asked that they should be paid. This was refused, however, and the bills dishonoured. He then sued the bank, and obtained a verdict in his favour, with damages for injury to his credit. It was decided by the jury that the plaintiff was entitled to a reasonable notice before the closing of his account, and that such a notice had not been given.

If a cheque is presented to a banker for payment and there are not sufficient funds to meet it, owing to the banker having debited the customer with his charges for keeping the account, it would not be wise for him to return the cheque unpaid, unless the customer has received notice of the charge. But should it be shown that the charge was a customary one, debited periodically to this particular account, it is probable that the banker would not be held liable for returning the cheque.

If a banker receives a "garnishee order," he is entitled to refuse payment of all cheques presented after receipt of the order, although the balance in his hands may exceed that attached by the order. A "garnishee order" is an order granted to a creditor who has obtained judgment against his debtor, attaching "all debts owing or accruing due" from a third person to the debtor. In the case *Rogers* v. *Whiteley*, the plaintiff had a banking account with the defendant bankers, upon whom a garnishee order for £6000 was served at a time when the plaintiff's balance was £6800. The defendants dishonoured cheques amounting to less than the surplus of £800, but the plaintiff was unable to sustain his suit for damages.

Besides the collection and payment of cheques for a customer who has a current account, a banker performs various other duties in the course of his business. In the first place, he receives money on deposit bearing interest. It is not the usual practice of English bankers to allow interest on current accounts, though sometimes interest on the minimum monthly balance is given by special arrangement.

English bankers, however, receive money repayable usually at seven days' notice with interest at a rate which is as a general rule 1½ per cent below the Bank of England discount rate. Cheque-books are not issued to those who have only a deposit account. Should the depositor wish to withdraw a part or the whole of his account without giving the stipulated notice, the banker is usually willing to do so, the customer forfeiting seven days' interest in lieu of notice. The deposit receipts issued by bankers are marked "not transferable," and are in all probability not negotiable instruments at all.

The collection of dividends, interest, and coupons is another duty undertaken by bankers. In the case of dividends on stocks or shares registered in the customer's name or inscribed in the books of the Bank of England, it is usual for the customer, if he wishes the dividends to be paid direct to his banker, to sign an authority requesting the company or the Bank of England to forward them as desired, and forms for this purpose can be supplied by the banker.

As a rule no company will recognise trustees as the holders of shares, which must be registered simply in the joint names. Neither will they as a rule pay over the dividends to the credit of a party other than the registered holders. If the dividends are to go to the credit of a third party, instructions should be given to the collecting banker and not to the secretary of the company. In collecting coupons, the customer may either keep the bonds in his own possession or in a box at the bank, and cut off the coupons himself before handing them to the banker for collection, or he may lodge the bonds with his banker, when the latter will himself cut off and collect the coupons. When bonds are so deposited with a banker, he will usually watch the results of the drawings if they are redeemable by lot and inform the customer, but it is not certain whether a banker is liable to the customer for neglect of this. If the customer cuts off his own coupons, he should hand them to the banker not later than a fortnight before they fall due, if he wishes for the prompt receipt of the proceeds. Should coupons be payable abroad, it is usual for bankers to sell them in London to an agent when possible. Income tax on coupons is always deducted by the banker who collects them.

Bankers accept "standing orders" from their customers to pay subscriptions to clubs, charities, and similar institutions; they will also remit money abroad or collect drafts payable abroad. When lodging with a banker for collection bills payable abroad, a customer should always give full instructions as to the course to be followed in case of dishonour, and should documents of title be attached to the bill, whether these documents are to be surrendered to the drawer upon acceptance or upon payment. Bills with such documents attached should be drawn to the order of the shippers and endorsed in blank.

Another function of bankers is the issue of "Letters of Credit" and "Circular Notes." A Letter of Credit is a request from one banker to a correspondent or agent authorising him to honour the drafts of the person named in the Letter of Credit, and promising to pay such drafts when presented. The correspondent is usually advised that such a Letter of Credit has been issued to a third person, and a specimen of the latter's signature is forwarded for the purpose of identification. When the correspondent makes any payment under a Letter of Credit, he endorses the amount on its back and usually charges a small commission to recoup himself; in some cases, however, he draws upon the issuer for the amount of the commission. A Circular Letter of Credit is one addressed to a series of correspondents named in another document called a "Letter of Indication."

"Circular Notes" are drafts drawn by bankers for a round sum, usually £10, upon a number of foreign correspondents, in favour of the customer to whom they are issued. The drawees are in this instance also enumerated in a letter of indication, and as this contains the specimen signature of the payee, it should not be kept in the same receptacle with the Circular Notes when travelling, so that in case of loss or theft the one will be useless to the finder without the other, and forgery be less easily accomplished.

Among the minor duties which a banker is called upon to fulfil may be mentioned the custody of bills not due which a customer does not wish to discount; such bills are called "Short Bills," and the banker presents them as they fall due, without special instructions from the customer, and credits the proceeds to the account.

If the holder of a bank-note accidentally destroys or loses it, he can on reference to his banker obtain a form of indemnity, on receipt of which, properly executed, the Bank of England will pay the amount of such notes.

Customers can also buy and sell stocks and shares through their banker. Nothing but the usual broker's commission will be charged; but the banker usually arranges with the brokers whom he employs to halve such commission with him. A banker will not as a rule undertake the responsibility of advising his customers as to investments.

Finally, a banker will take charge of boxes or parcels for his customers and hold them on safe custody. For this a banker makes no charge, neither does he take any cognisance of the contents of the boxes, which should be securely locked or sealed. In doing so a banker acts as a bailee and not "as a banker," and his liability in case of loss, damage, or delivery to the wrong person has not yet been settled. A case came before the courts in 1896, but was settled by a compromise, and no legal precedent was therefore made.

In this case, *Langtry* v. *The Union Bank of London*, the plaintiff lodged with the defendant bank a box containing jewels stated to be worth £35,000. This was delivered by the bank to an unknown person on a forged order. Thereupon Mrs. Langtry sued the bank, and by a compromise out of Court it was arranged that verdict should be given for the defendants on payment by them of £10,000.

The fact that the bank did not fight the case points to the belief that their position was a weak one. The opinion given by the Central Association of Bankers, after due consideration of the case, is that if valuables deposited with a bank for safe custody are lost, stolen, or destroyed by fire, the banker is not liable unless negligence can be proved against him. If he took such reasonable precautions as a prudent man would take in the case of his own valuables, he would be held exempt from liability. If, however, the banker delivers them on a forged order, it would probably be held to be wrongful conversion of the goods, and the banker would be liable apart from any question of negligence. The Central Association goes on to recommend the adoption of a form of receipt for such valuables, with a blank order for delivery printed on the back. If the banker refused to deliver the valuables except on the production of such receipt, it would make it more difficult for a fraudulent party to obtain possession.

Advances and Security.—A banker lends money in various ways and on various kinds of security. In the first place he discounts bills for a customer; that is to say, a banker buys a bill which is due at a future time and gives his customer immediate credit for the amount of the bill, charging on the transaction what is called by bankers "discount," which, however, is not true discount but interest. That is to say, if true discount were charged the net amount which is credited to the customer should be such as with interest at the arranged rate would equal the nominal amount of the bill. But the banker charges interest on the full amount of the bill and gains by doing so the interest on the discount.

The rate of discount which is officially quoted by the Bank of England, and is known as the "bank rate," is the rate for what are called "first-class"

bills only; that is to say, bills accepted by parties well known in the City of London and on which there is the minimum of risk attaching.

It cannot be expected that a banker shall discount ordinary trade bills at this rate, as he has to provide against the danger of the bill proving worthless. A banker takes the state of his customer's account into consideration, and if the account is not well kept he may, and frequently does refuse to discount the proffered bill. If he decides favourably he will next make a confidential inquiry of the banker with whom the bill is domiciled, and on the nature of the answer will depend his final decision. Bankers often keep an "Acceptor's Book," in which are kept any particulars they may acquire of the acceptors of bills which periodically pass through their hands. As ordinary trade bills frequently recur through the same channels a banker gradually acquires some knowledge of the parties whose acceptances he discounts. Should one be dishonoured the particulars of it and the answer on it will be duly registered in the "Acceptor's Book" and he will, if he think fit, refuse to discount any more accepted by the same party.

The class of bills which a banker prefers to discount are those which are customarily drawn in certain trades, chiefly by manufacturers and wholesale dealers upon the retailer. In some trades it is customary for the retailer to pay for the goods he buys by means of bills at a certain recognised currency, frequently three months. Unless the manufacturer has a large capital he finds it preferable to discount these bills with his bankers, and such bills are as a rule readily accepted by the latter. This custom of paying by means of bills is, however, slowly giving way to payment by cheques, and the number of trade bills in circulation is very much less than was the case twenty or thirty years ago. There is another class of bills which is not so satisfactory to a banker, those drawn by private individuals in payment of goods or ordinary household expenses; these usually indicate shortness of money on the part of the acceptor and an anticipation of his ordinary sources of income, and are to be looked at with caution. The third class of bills is generally avoided by bankers altogether when they are recognised, though this is not so easy; these are accommodation bills. If a man accepts a bill for the accommodation of another without receiving value for it, he is nevertheless liable to a holder in due course, though there is usually an implied contract that the accommodated party shall provide for the bill before presentation. As a rule a man does not borrow money by means of an accommodation bill until the ordinary methods are exhausted, and so this class of bills is looked upon with suspicion. A banker is never certain how far this method of accommodation may extend, and it is a matter of no great difficulty for three or four individuals to combine and mutually accept bills drawn upon each other without any business transactions between them and without capital or resources. Such a course of procedure may attain very large proportions before it is found out, and then probably a crash will ensue. The commercial crisis of 1857 was attributed at the time to the extensiveness with which accommodation bills were created among foreign firms who drew on agents in London. These agents accepted bills drawn on them without value passing, on payment of a commission and on the understanding that they should be paid before maturity; "acceptances on open credit" they were called, and they were usually paid by the substitution of a fresh set of bills; this continued until the crash came and a panic ensued. Experience only will teach a banker to distinguish accommodation bills, but they are generally drawn for round sums and at as long dates as bankers will accept.

Bankers prefer to discount bills drawn at short dates, as there is not so

much time for the position of his customer to change, and he can consequently more easily alter his policy in dealing with him if he should begin to distrust his financial position; many banks refuse to discount bills having more than six months to run. A banker always requires his customer to endorse bills before discounting them, otherwise he would have no recourse against him if the bills were unpaid. A banker is not acting as his customer's agent when he discounts bills; he buys the bills and becomes a holder for value, and as such claims on his customer as endorser in case of dishonour.

Of course, in lending money by means of discounts, a banker requires no further security beyond the bill; the transaction is complete in itself; he has, first of all, the right against the acceptor of the bill; if this fail he has the right against his customer as endorser and perhaps as drawer; if the bill is drawn by a third party he has a further recourse against him as drawer.

A second method of lending money is by means of promissory notes; a banker will often, in the case of a customer of good standing, advance money to him by discounting his note of hand for a short period, say three or four months. He may require his customer to produce a third party who will join with him in a "joint and several" promissory note, in which case the banker has a right against each of them for the full amount of the bill. The advantage to the customer of borrowing money in this way is that the debt cannot be recalled before the maturity of the note. The banker buys a future right when he discounts the note, and until the latter matures he has no right of recourse against his customer. The advantage to the banker is that the customer is expected to keep some part of the proceeds to his credit, or else he will be required to pay a further commission on the management of his current account, should the balance kept prove unsatisfactory.

Besides these two methods of lending money, a banker can grant his customer a loan or a "cash credit," as it is called in Scotland, or he may allow him to overdraw his current account.

In the former case a separate "loan account" is opened in the customer's name and an arrangement is made as to the amount which may be drawn on this "loan account." Amounts are then transferred from this account to the current account as the customer requires them, and he repays them at his convenience, subject, of course, to the arrangements made with the bank manager. As a general rule the bank retains the right to demand payment of the whole amount when it considers necessary. If a customer has a loan he is usually expected to keep a sufficient balance on his current account to remunerate the banker, the amount of which, of course, varies with the character of the account. If the customer prefers an overdraft, he becomes entitled to draw until he has a debit balance to the extent agreed upon. In this case he pays interest on his debit balance and a commission to cover the expenses of managing his account; in a loan account no commission is as a rule charged, as the customer is still required to keep a credit balance. In dealing with these two methods of lending money, we have to discuss the question of security. Of course there are cases in which a banker feels sufficient confidence in his customer to advance money temporarily without security, but these cases are exceptions.

Briefly speaking, the essentials of an ideal banker's security are not so much ultimate security as immediate convertibility. Advances at short dates on convertible security constitute the class of business most sought after. A banker does not aim at providing capital wherewith a man shall

trade; he chiefly desires to tide a man over temporary want of available assets, or to give a man the means of making a successful start in business. A banker's liabilities are nearly all to pay gold on demand, and he cannot afford to lock up his assets more than is necessary. Many a banking catastrophe has been occasioned, not by insolvency but by temporary lack of available assets due to bad business management.

The most general form of security which a banker possesses is afforded by the lien which he holds on all negotiable instruments deposited with him as a banker. A lien is a right to retain an article of value pending the payment of a debt due. This may be a "particular lien"; that is to say, it may attach to an article only until the debt due on that individual article is settled: all tradesmen possess a particular lien on an article deposited with them for repair or for any purpose necessitating the expenditure of money or labour. A "general" lien attaches to articles in possession of the debtor as against all debts due, however incurred. This "general lien" is possessed under the common law by bankers, brokers, factors, innkeepers, solicitors, and wharfingers.

This general lien implies the right to retain but not the right to sell, and it attaches in the case of bankers only to such articles as are deposited with them *as bankers;* thus it was held in the case of *Brandao* v. *Barnett* (1846) that securities lodged with a banker for the sole purpose of being held by the latter on safe custody are not subject to the banker's lien. The plaintiff's agent, named Burn, kept an account with the defendants and had several tin boxes in which the securities of his principals were lodged with the bank for safe custody; he was in the habit of taking these out from time to time and handing them to the banker for the collection of interest due. On one occasion when exchequer bills amounting to £10,000 were so dealt with, Burn, owing to illness, omitted to replace them in the box and left them in the hands of the bank. Burn was then made bankrupt and the bank claimed a general lien on the exchequer bills to secure the payment of the overdrawn account. The House of Lords, however, held that the lien did not attach to the bills because they were left with the banker with the intention of being replaced in the box for safe custody and that therefore they were not held by the defendants as bankers, but as bailees; there was no *duty* imposed upon the banker of collecting the interest upon these bills, which had been taken from the box by the plaintiff and handed to the banker for a special purpose.

It is, however, a general practice for the customers of a bank to entrust to them bonds, certificates, scrip and such securities, not only for safe custody, but in order that the banker may collect the dividends as they fall due without special instructions from the customer; in this case it seems clear that it is the duty of the banker as such to duly collect the interest, and bank prospectuses often contain clauses expressing their willingness to undertake this class of business. If such is the case, these securities are lodged with the bankers in the ordinary course of a banker's business, and, if so, the general lien of a banker will attach to them.

The general lien of a banker attaches also to cheques deposited with him for collection, and to bills deposited for discount, or held by the banker "short," but it does not extend to plate and jewellery held in his strong-room on the customer's behalf. If a customer has several accounts with a banker or accounts at several branches, the general lien covers all of them and the banker enjoys the right of "setting off" one against the other; should one of the accounts, however, be a trust account and the banker be affected with notice that this is so, this will not be covered by the banker's lien

Besides his general lien a banker may create a conventional lien, or lien based on an agreement between himself and his customer, and when the two are inconsistent a conventional lien is held to override the general lien. A banker often lends money on securities which he accepts under a "memorandum of deposit," which is an ordinary agreement, stamped with a 6d. stamp and generally granting the bank a power of sale. In the case, *in re Bowes, Earl of Strathmore* v. *Vane*, Bowes deposited a life policy for £5000 under such a "memorandum of deposit," which stated that the policy was lodged to cover advances not exceeding £4000. Bowes died and the bank claimed a general lien on the policy for the full amount, but it was held that the general lien was excluded by the terms of the conventional lien created by the memorandum.

Securities deposited with a banker to cover an advance may either belong to the debtor or they may be "collateral." A collateral security is obtained by the pledge of valuables belonging to a person other than the debtor. If a banker holds collateral security he can, in the event of the bankruptcy of the debtor, claim against the estate for the whole of his debt and then realise his security to satisfy the remainder of his claims. If, however, the securities pledged are the property of the debtor, they must be realised before the banker claims on the estate, and his claim can only be for the balance of the account remaining. The private property of a partner pledged to secure the debt of the firm constitutes a form of collateral security.

The first form of security to be considered is that of the deeds of title to land. Although this is generally considered one of the most desirable forms of security, it has the drawback from the banker's standpoint that it cannot always be readily realised. A banker will not as a rule accept a second charge on landed property as security for an advance, and if he is prudent he will insist on the deposit of the title deeds, which should be submitted to a solicitor and a report obtained as to their genuineness and the validity of the holder's title. He may then either take a legal mortgage or they may be deposited under a memorandum of deposit, which constitutes an equitable mortgage. The memorandum should contain a clause stating that the deeds are to secure future as well as existing advances, otherwise, as we have seen above, the original advance may be held to be paid off by the first entries on the credit side of the account, and a new advance contracted, although there may have been a continuous debit balance. This is called the "general rule as to the appropriation of payments."

It is also advisable to have a clause binding the depositor to give a legal mortgage when called upon. The rule of the courts is that a legal mortgage has priority over an equitable mortgage. If, however, the banker retains the title deeds it is hardly possible for a legal mortgage to be created; caution should therefore be used in parting with deeds deposited under a memorandum, even though they should be required for a short time only.

If the banker receives notice of a contract of sale of land on which he holds an equitable mortgage, he should at once stop the account and make no further advance on the security. In the case of *London County Banking Co., Ltd.*, v. *Ratcliffe*, the bank continued to make fresh advances after such notice, and it was held in the House of Lords that no charge on the land was created by such advances after notice of sale, and that the original advance had been extinguished by the payments made by the defendant to the credit of his account since the date of the contract of sale. It may be mentioned that the mere deposit of title deeds without a memorandum constitutes an equitable mortgage. The disadvantage of a second charge

on landed property is that, by what is known as "tacking," the holder of a third mortgage may under certain circumstances join his charge to that of the first mortgagee, and the two together take precedence of a second mortgage, the holder of which finds himself in a considerably worse position than he anticipated.

The second form of security to be considered is that of stocks and shares. This is perhaps the largest class of securities with which a banker deals, and the debentures of a first-class company—a "gilt-edged" security, as it is called—are perhaps one of the most satisfactory a banker can possess. Bankers do not care to advance money on mining shares and similar speculative undertakings, nor do they look with favour on shares which are not fully paid up, and a banker usually requires a considerable margin on the value of the securities to cover fluctuations in the market price.

With the exception of bearer-bonds and certain forms of scrip, which are transferable by mere delivery, all stocks and shares require to be transferred into the names of the banker or his nominees before a legal title to them can be obtained; such transfer must be registered with the company. If the transfer is not so registered, not only does the banker get no legal title, but his charge on the stock or shares may be postponed to a subsequent charge in favour of the company. Two cases are of special interest to bankers in this connection. In *The Bradford Banking Company, Ltd.*, v. *Henry Briggs, Son, and Company, Ltd.*, the bank obtained from a customer named Easby the deposit of certificates of a number of shares in the defendant company; they were not transferred into the bank's name, but notice of the deposit was given to the defendants, who, in acknowledging the receipt of the notice, wrote to the bankers as follows:—"We think it right to inform you that Mr. Easby is indebted to us, and that under a clause of our Articles of Association we have a first and permanent lien upon all shares held by him." The bank, however, proved that they had made no fresh advance to Easby since the shares were deposited, but that, on the other hand, the debt of Easby to the defendants had been paid since that date, and fresh ones contracted. For this reason judgment was given for the plaintiffs, on the ground that the defendants had received notice of the bank's charge on the shares, and that any subsequent advance by the defendant company only created a second charge on the shares, over which the charge of the bank took priority. The other case is *Powell* v. *London and Provincial Bank*. A man named Edwards was registered in the books of the Penarth Harbour Company as holder of £1000 stock, which was in reality held by him in trust, although, in accordance with custom, no note of the trust was made in the company's books. He deposited the certificate of this stock with the defendant bank as security for a loan, assuring them that he was the true owner. The deposit was made under a memorandum, in which Edwards promised to transfer the stock when called upon, in order to complete the bank's title. At the same time a signed transfer, with blanks for the name of the transferee, was executed by him. Some years after, the bank wrote to Edwards that, unless he reduced the advance, the stock would be transferred. This was done, and the stock was afterwards sold by the bank with the consent of Edwards. He eventually absconded, and when new trustees were appointed in his place, they brought this action against the bank for the amount of the stock and the dividends received by the bank in reduction of their advance by Edwards.

Judgment was given for the trustees on the following grounds:—

(1) No legal title to stock and shares can be acquired unless the stock

is transferred by deed executed by the transferor, and registered in the books of the company.

(2) Registration alone without transfer gives no legal title.

(3) The transfer executed by filling up the blanks left in the form was not a complete transfer, because it had not been redelivered after the blanks had been filled in.

(4) The bank had not acquired a legal title to the stock, and therefore their equitable title was postponed to the prior equitable title of the trustees.

Bonds to bearer are negotiable instruments transferable by delivery, and therefore the mere deposit of them for valuable considerations is sufficient to give a good title to a bank, provided they are taken in good faith and without knowledge of any defect in the title. It is necessary to note, however, that if the coupons are not attached to the bond, it is not a negotiable instrument.

The question as to what is knowledge or notice of defect, in the title to negotiable securities, received a curious solution in the case of *The Earl of Sheffield* v. *The London Joint-Stock Bank*. The bank advanced money on the deposit of, among other things, bonds to bearer by a customer who was a money-lender, and the House of Lords held that the bank was bound to inquire into the title of the pledger, knowing that he was in the possession of securities belonging to third parties. Lord Halsbury's opinion was as follows:—"The conclusion I draw from the facts proved, is that the bank knew very well the system of money-lending pursued by Mozley, and trusted to him that he would not over-pledge, so to speak, the securities of his customers. . . . If that be the true view of the facts, it is impossible to contend that the bank is entitled to the position of purchasers for value without notice. I think they had actual knowledge; but if they had reason to think the securities might be Mozley's own, or might belong to somebody else, I think they were bound to inquire." Lord Sheffield, to whom the securities belonged, claimed the right to redeem them for the sum actually advanced on them by Mozley, and this relief was granted by the House of Lords.

As to what classes of securities are to be considered negotiable instruments, since they are not defined by common or statute law, the custom of merchants is held by the Courts to determine the question of negotiability. In this connection it was held in *Picker* v. *The London and County Banking Company, Ltd.*, that it is not sufficient to prove that foreign bonds are negotiable in the country in which they were issued, but that negotiability in this country can arise from the custom of *English* merchants and business men only.

Another form of security for advances for a banker is a "guarantee" given by a third party. This, of course, is collateral security, and possesses the advantages of this class of security in the event of the bankruptcy of the borrower. A guarantee is an excellent form of security if the banker has thorough and trustworthy knowledge of the means of the guarantor, otherwise it is of uncertain value and may prove quite worthless.

A guarantee may be drawn on a sixpenny impressed stamp, unless it is made under seal, when an *ad valorem* impressed stamp is required. It may be individual, or joint and several, and if made by a firm each partner should sign separately. It should express the time till which it is to remain in force, or else, as is more usual among bankers, should be a continuing guarantee for the payment of "all money from time to time owing," with interest, commission, and other banking charges; and should

then further express the notice required for the guarantor to release himself from liability: the usual notice is six months.

Bankers sometimes make advances upon life insurance policies, though it is an unsatisfactory form of security, and no advance should be made exceeding the amount of the surrender value.

Finally, we have to consider the advances made by bankers upon documents of title to goods. This is a class of security which is largely in vogue in shipping circles, but is very seldom met with outside such circles. Under the Factors Act, which we shall shortly consider, bills of lading, dock warrants, delivery orders, and warehouse-keepers' certificates are all considered to be documents of title; but, speaking strictly, the first-named is the only true document of title, the transfer of which is equivalent to a delivery of the goods.

A bill of lading is defined by Lord Blackburn as "a writing signed on behalf of the owner of the ship in which goods are embarked, acknowledging the receipt of the goods, and undertaking to deliver them at the end of the voyage (subject to such conditions as may be mentioned in the bill of lading).

As long as goods are at sea, or are held by the master of the ship under lien for unpaid freight, a bill of lading is the symbol of the goods themselves, and the endorsement of a bill of lading to another person transfers the property of the goods and the right to sue on them. It would appear, therefore, that bills of lading are negotiable instruments, since they are transferable by endorsement and delivery, and confer the rights above mentioned. But the holder of a bill of lading cannot, except under certain circumstances, pass to an endorsee a better title to the goods than he himself possesses: he only transfers the right to obtain possession of the goods, but does not necessarily transfer a good title. For this reason a bill of lading is called a quasi-negotiable instrument. It is a general and almost universal custom to draw bills of lading in sets of two or three, and a banker should take care to obtain possession of all the parts of a set before making an advance upon it, otherwise he may find himself fraudulently deprived of his right to obtain possession. It was settled in *Meyerstein* v. *Barber* that when two or more parts of a set are negotiated to different holders, the title of the transferee who is first in point of time prevails over that of a subsequent transferee; but a master or warehouseman is justified in delivering the goods to the holder who first presents one of a set. It would appear from these facts that a bill of lading is a poor form of security for a banker, because his title to the goods depends upon that of the transferor; but he is protected to a great extent by the provisions of the Factors Act. A great deal of the business connected with the shipping of goods and consigning them for sale is done through "mercantile agents" or "factors," and as there are necessarily many opportunities for fraud, and few means of recognising the true owner of such goods, the Factors Act steps in to protect those who have dealings with such agents. "Where a mercantile agent is, with the consent of the owner, in possession of goods or of the documents of title to goods, any sale, pledge, or other disposition of the goods, made by him when acting in the ordinary course of business of a mercantile agent, shall, subject to the provisions of this Act, be as valid as if he were expressly authorised by the owner of the goods to make the same; provided that the person taking under the disposition acts in good faith, and has not at the time of the disposition notice that the person making the disposition has not authority to make the same" (Factors Act 1889, clause 2). Under the provisions of this Act, not only bills of lading but

dock warrants and delivery orders are documents of title, and the pledge of such documents is deemed to be a pledge of the goods. A dock warrant is a document issued by a dock-keeper, stating that certain goods are held by him deliverable to a person named. A delivery order is an order issued by the owner of goods to a dock-keeper, requesting him to deliver the goods to a person named. The unpaid vendor of goods has the right of stopping the goods "in transitu," in case the buyer becomes bankrupt before obtaining possession of the goods; but if the documents of title to the goods have come into the hands of a third party, who took them for valuable consideration and without notice, this right of stoppage is defeated. If, then, a banker advances money on documents of title to customers whom he knows to be brokers or factors, he is in most cases protected from the results of any defect in the pledgor's title. It is necessary to state, however, that the master of a ship undertakes no responsibility as to the contents or quality of the goods he ships, and merely acknowledges the receipt of so many packages. The banker advancing on bills of lading is therefore somewhat at the mercy of the shipper.

A banker often advances money on bills of lading by buying bills of exchange drawn on the consignee with the bills of lading attached. The bill is of course not accepted at the time the banker takes it, but the bill of lading is security for the payment of the bill of exchange, and the former is not delivered to the consignee until the latter is paid or at least accepted, according to instructions.

The Outlook.—Before closing, we must glance at the present condition of banking and the outlook before us. Perhaps the most striking feature of recent banking is the fact that for thirty-four years we have had no panic and no failure among the larger banks. One reason for this may be that until the last few years prices have been, generally speaking, on the downward grade, and speculation has been wanting. Speculative trade and the over-inflation of credit are the primary causes of commercial and banking crises; prices are artificially raised, and a semblance of unusual prosperity lulls people into security, until the bubble suddenly bursts, and in the reaction a general loss of confidence threatens danger to the foundations of our financial system. Experience has taught our larger commercial firms to work on a more secure basis than formerly; they are better capitalized, keep larger reserve funds, and conduct their business on more cautious lines. Speculation has certainly at times been rampant, as witness the South African boom in the early 'nineties, but the speculation has been open and recognised as such, and has been confined to certain limited classes. Another reason for our continued safety is to be found in the better administration of our banks. There has been a strong tendency towards the evolution of a more powerful class of bank, with more capital and a better reserve fund than their predecessors; all joint-stock banks and most private banks issue balance sheets, and the increased publicity tends to a steadier business tone. But yet our utter dependence on the Bank of England is unsatisfactory. The bank still holds the premier position by virtue of its reputation, its position as the Government banker, and as the holder of the reserve; but as regards the volume of business done it is outclassed by several of the leading joint-stock banks, and yet these powerful rivals of the bank are dependent upon it for all supplies of gold beyond what suffices for times of commercial peace. Yet when we look at the recent tendency of modern banking we wonder if there is any chance of reform in this direction. Branch banks are springing up almost in every street in London, competition is almost as acute in the country,

and the expenses of management seem to be increasing at a quicker rate than earnings. Under these circumstances the prospect of the leading joint-stock banks voluntarily saddling themselves with the incubus of keeping a cash reserve does not seem attractive. London bankers now keep their reserve cash either at the Bank of England or on short loan—that is, money lent on call or repayable on short notice to stock and bill brokers. The money lent to the Bank of England is a liability of the bank to that extent to pay gold when called upon, and if the London bankers withdrew their deposits in gold it would drain the bank of almost the whole of its reserve bullion. Moreover, it is calculated that from thirty to forty millions sterling of English bills are held by foreigners abroad, and these all incur liability to pay gold. If at a time when the bank reserve was low a large proportion of these bills had to be liquidated in gold, we can easily see that the result might be extremely disastrous, as the reserve of the bank does not exceed on the average twenty millions.

It is at first sight a matter of surprise that London is the great market for gold for the whole world, and yet her reserve of gold is considerably less than that of France, Russia, or Germany. This fact is explained, however, when we consider that London is the one free market for gold, and that no hindrances are placed on the export of gold. Consequently it is difficult to restrain a foreign drain. The only method of inviting gold is to raise the rate of discount, a rate which is only in part controlled by the Bank of England. The consequence, however, of raising the rate is to limit credit in England, and to hinder productive enterprise, so that it is a power which needs delicate handling. The fact that the London bankers keep their balances with the Bank of England enables the latter to use these in the creation of credit, by which the liability to pay gold is also increased. If these reserves were kept in the bankers' own cellars, not only would there be a reserve in London which would enable the banks to meet all ordinary demands independently of the Bank of England, but the liability of the Bank of England would be so much less, and she would be in a better position for meeting the foreign demands. Of course we should have to pay for this by the loss accruing from the idleness of capital represented by the reserves of the banks, but if it is true that we are sailing too close to the wind, and that our position is not secure enough, this is unavoidable.

It has often been suggested that we should provide an ultimate reserve for use in the emergency of a panic by following the example of Germany in dealing with her note issue.

Every note issued by the Bank of England beyond the £17,750,000 issued on securities has to be secured by the deposit of gold to a like amount in the issue department. In Germany the bank is allowed to break this rule and issue without the deposit of gold on payment of a fine of five per cent, and this power is frequently used, the fines in the year 1898 amounting to £96,370. If adopted in England this would set free a fund amounting on the average to nearly ten millions for use on emergency, but it would not strengthen our position in ordinary times. It would only prevent what happened in 1847, 1857, and 1866, when the Bank Act had to be suspended and recourse had to an Act of Indemnity.

Of course it would be a matter of time for our joint-stock banks to collect cash reserves of their own; any attempt to provide them hurriedly would utterly derange the money market, but it would be rendered easier by the greater unanimity which would prevail between the interests of the Bank of England and the other banks. Formerly the market rate of

discount was controlled by the Bank of England rate, but such is by no means the case now. The bank is overshadowed at times by her larger rivals, and the bank rate is forced down by the latter below the point which the bank considers necessary or safe, because the joint-stock banks are more concerned in getting their spare cash on to the market than in protecting the Bank of England reserve. If all shared the liability of keeping a reserve, there would be a community of interest and a general combination to take such measures as are necessary for safety. Such combination occurs now only in the face of immediate danger, as in the joint guarantee of Barings by the clearing bankers in 1890, but it takes time to materially increase our stock of gold, and such combination is, under present circumstances, too late for security. We want a greater community of interest and sharing of responsibility in times of commercial peace.

For those who wish to pursue the study of banking at greater length the following works are suggested:

History and Theory of Banking: GILBERT'S *History, Principles, and Practice of Banking.* Edited by A. S. Michie.—H. D. MACLEOD'S *Theory and Practice of Banking.*—W. BAGEHOT'S *Lombard Street.*—C. M. COLLINS. *The Law and Practice of Banking in Ireland.*—ARTHUR CRUMP. *The English Manual of Banking.*—JOHN DUN. *British Banking Statistics.*—T. HANKEY. *Principles of Banking.*—W. S. JEVONS. *Money and the Mechanism of Exchange.*—A. W. KERR. *History of Banking in Scotland.*—R. H. INGLIS PALGRAVE. *Dictionary of Political Economy.*

The following Parliamentary Papers can also be consulted with advantage:—*Report of the Select Committee appointed to inquire into the high price of Bullion, 1810. Report of the Select Committee appointed to inquire into the renewing of the Bank Charter Act 1832. Report of Select Committee on Banks of Issue, 1840. Report from Select Committee on the operation of the Bank Acts of 1844 and 1845. Report of Select Committee on Banks of Issue, 1875.*

The Practice of Modern Banking: *Journal of the Institute of Bankers.*—*Questions on Banking Practice* (published for the Institute of Bankers).—*Legal Decisions affecting Bankers* (edited by Sir John Paget).—T. B. MOXON'S *Practical Banking.*—J. HUTCHISON. *The Practice of Banking.*

ERNEST SYKES

FOREIGN BANKING

By R. H. CARY

Foreign Banking

Banking in the United States

Historical.—The early history of banking in the United States is not very pleasant reading. Indeed, if we go back to colonial times, we find that the greatest stumbling-block to the best intentioned government was that of the currency. From the first issue of paper money by the colony of Massachusetts in 1690, a batch of bills to pay the army just returned from a fruitless expedition against Canada, nearly every colonial governor was at variance with his legislature concerning paper money. Indeed, it appears that intolerance of restraint from the mother country on this subject was a very sore point with the colonists, although as one of the causes which finally led to separation it has received scant recognition from our own historians, but has been duly appreciated by those of America.

Of the earlier banks there are three which still occupy prominent positions, viz. the Bank of North America, founded at Philadelphia in 1782; the Bank of Massachusetts, founded at Boston 1784; and the Bank of New York, founded in the same year in the city of that name. Their charters do not mention anything about the issue of notes, as the right of issue in those days needed no authorisation.

The first "Bank of the United States" was chartered in 1791 for a term of twenty years, with a capital of $10,000,000. It had a successful career, during which it rendered good service alike to the Government and the currency, but finally it fell a victim to its enemies, mostly politicians, and a renewal of its charter in 1811 was refused. The bank thereupon went into liquidation, paying its shareholders about $430 for each $400 share.

To fill the void left by the Bank of the United States a large number of State banks immediately sprang up, but in the dark days of 1814 nearly all suspended payment. The war having come to an end, the question of a second Bank of the United States was brought forward, and after much opposition was chartered in 1816 for a term of twenty years, with a capital of $35,000,000. Almost immediately it fell into difficulties through lending largely on the security of its own shares, a banking practice which is generally condemned, for if the debtors default it is plain that the bank's capital is gone.

By good management, however, the second Bank of the United States retrieved its position, but nevertheless at the expiry of its charter it was not granted a renewal, and there is now no 'Bank of the United States."

It gradually sold its branches which it could no longer legally retain, and in February 1836 started on a new career as the United States Bank of Pennsylvania, having been granted a charter for thirty years by the legislature of that State. The commercial disasters which fell upon the

country during the next few years caused the bank, among hundreds of others, to suspend in 1837, again in 1838, and finally to close its doors in 1841. The creditors were paid in full, both principal and interest, after many years of liquidation, but the shareholders lost all. Nicholas Biddle, the famous president of the bank died, poor, discredited, and broken-hearted in 1844. Without doubt Biddle was the most remarkable man of his time. At the height of his career his bank parlour might have been taken for the *salon* of a potentate, as indeed he was of the banking world of America. Men ran after him, fawned upon him, until it became quite an open question whether he or the President of the United States was the greater man.

Mr. Horace White says in *Money and Banking*, 1896:—"If it (the Bank) had gone into peaceful liquidation (1836), like its predecessors, its shareholders would have blessed instead of cursing it, its friends would have been justified, and its enemies confounded. Nicholas Biddle would have passed a serene old age, and would have been considered by posterity the nation's greatest banker. If the bank had curtailed its capital to the amount that could be profitably used in its new sphere and in the changed conditions which were coming, and had paid the excess back to its shareholders while it could, it might be living to-day alongside the Bank of North America and the Girard Bank, its elders and its neighbours. Pride would not allow this giant among banks to reduce its size to correspond with its new place and belongings. Mr. Biddle, after filling so large a space in the world, could not shrink to his proper dimensions."

"The heterogeneous state of the currency in the fifties can be best learned from the numerous bank note 'reporters' and 'counterfeit detectors' of that period. It was the aim of these publications to give early and correct information to enable the public to detect spurious and worthless bank notes, which were of various kinds. Disputes between payer and payee as to the goodness of bank notes were of frequent occurrence at that time, ranging over the whole gamut—whether the issuing bank was sound or unsound, whether the note was genuine or counterfeit, and if sound and genuine whether the discount (depreciation of the note) was within reasonable limits.

"All merchants kept *Bank Note Reporters* for ready reference. These manifold evils were chiefly due to want of uniformity and of public regulation. Want of uniformity opened the door to the 5400 counterfeit and spurious notes catalogued at one time. When the national banking law went into full effect the *Bank Note Reporters* ceased publication. There was no longer a demand for them, because the evils which they were intended to guard against had for the most part disappeared."

MODERN BANKING.—According to the returns for 1902, the banking system of the United States is composed of 417 Loan and Trust Companies, 1039 Private Banks, 1036 Savings Banks, 5397 State Banks, and 4601 National Banks.

The Loan and Trust Companies are the product of the modern speculative spirit, and like the various syndicates which have grown up, are prepared on terms to undertake finance from which a city banker would stand aghast. These trusts are a source of great uneasiness to the New York banking world.

The Private Banks, as their title indicates, are ordinary private partnerships formed for practising the usual legitimate functions of ordinary banking; they are mostly small institutions.

The Savings Banks have been established for a great many years, and

upy a much more prominent position, and perform much more valuable services than the savings banks of the United Kingdom. Their object is to encourage thrift among and to help the poorer classes. The very smallest sums are received; some banks even accept deposits of 10 cents, others fix the minimum at $1. Interest begins to accrue at $5, and with between four and five millions of depositors, it will be readily understood that the total deposits are very large, amounting in fact to $2,650,000,000, the figures for State Banks at the same date being $1,698,000,000. The Savings Banks lend money to State governments and municipal corporations.

The banks of different States are, of course, subject to different regulations. The following particulars apply to the Savings Banks of the State of New York.

(*a*) Any thirteen or more persons may organise a bank. There is of course no share capital. The depositors are the shareholders, and their deposits form the capital; the profits therefore belong to them.

(*b*) The bank is governed by a board of trustees, who must meet at least once a month, and are not permitted to receive salaries, but those trustees who may be appointed officers, and therefore compelled to render regular attendance and service, may be remunerated accordingly, but are not allowed to vote.

(*c*) Investments are permitted in municipal and State bonds, and in real property to the extent of 65 per cent of the deposits. Not more than 10 per cent of the deposits may be kept uninvested.

(*d*) The trustees are prohibited from lending on notes, bills, or other personal security.

(*e*) The issue of deposit securities payable on demand is prohibited. Runs are thereby guarded against.

(*f*) The rate of interest allowed must not exceed 5 per cent.

(*g*) At least half-yearly reports must be rendered to the State authorities, and if two consecutive half-yearly reports be omitted the bank forfeits its charter and is wound up.

In some places the Savings Bank is conducted under the same roof and management as the State Bank or the National Bank, but for this arrangement there would be no Savings Bank in the town, and the inhabitants would not be able to enjoy the facilities and benefits offered by these institutions.

As stores of capital the Savings Banks are a great social force; public improvements are effected, and public needs satisfied without calling upon the ordinary banking capital of the nation.

The safety of the banks attracts a class of persons for whom they were not primarily intended, who frequently deposit large sums.

THE STATE BANKS are the oldest banks. They are not Government institutions, as their name might suggest, but simply banks which are organised under the special banking laws of the individual State in which they may be domiciled. These laws differ considerably in different parts of the Union, thus—

Four States require no reports from banks organised under their laws.

Six States require one report annually.

Thirty States require reports to be published in the local press.

Fourteen States prohibit note issues; several have no law upon the subject.

Twelve States make no provision for inspection by State officials.

Seven States have no restrictions on bank loans.

Twenty-four States lay down no requirements for the provision of a cash reserve.

Most of these banks are small, having a capital of $50,000 or less, but they supply a real want in the smaller towns. State legislation cannot compare with the national system as regards a sound and intelligent appreciation of the great principles involved in safe banking.

THE NATIONAL BANKS were called into existence by the Act of 1863 on account of the exigencies of the Civil War. The majority of the State Banks were established upon very insecure foundations, and such was the distrust engendered by them that great opposition began to be manifested to the existence of any banks of issue at all. In order to carry on the war it was necessary to find a market for United States bonds. Specie payments had already been suspended, and large issues of legal tender notes (sometimes called United States notes and "greenbacks") were made. These issues were regarded as a temporary, but unavoidable measure, and the establishment of the national banking system was intended to be the agency by which the sole paper issue of the nation was to be regulated in future. The National Bank note was designed to take the place of the greenback as soon as the latter should be paid, and an early return to specie payments was confidently looked forward to. But, according to Mr. John Jay Knox, late Comptroller of the Currency, *History of Banking in the United States*, "the National Bank note never was substituted for the legal tender note, and great as has been the benefit conferred on the country by national banks, this benefit is not that which was intended. The legal tender note has risen up and strangled the National Bank note at every turn, has prevented the development of the system, and has, by encouraging the issue of other forms of Government paper, left no field for an elastic bank currency. The triumph of the legal tender note might, however, have been expected. It is only another instance of the Gresham law, the worse currency driving out the better."

The original Act of 1863 has been amended from time to time, the latest changes being those made by the Currency Act of 1900. The following may be taken as the substance of the regulations which govern the national system at the present time.

1. The Comptroller of the Currency is the officer who presides over that branch of the Treasury which has charge of all matters concerning National Banks.

2. Any five or more persons may form an association for the purpose of carrying on the business of a bank; but the Comptroller of the Currency must grant his certificate (equivalent to a charter) before business can be commenced. The certificate runs for twenty years, and may then be renewed for twenty years. The Comptroller may refuse his certificate without assigning any reason.

3. If the population of a town does not exceed 3000 a bank may be opened with a capital of not less than $25,000. If the population is between 3000 and 6000, the capital must not be less than $50,000. If the population numbers between 6000 and 50,000, the capital must be at least $100,000. If the population exceeds 50,000, the capital must not be less than $200,000. One-half of the capital must be paid up before the doors of the bank can be opened, and the remainder must be paid in not less than monthly instalments of 10 per cent.

4. Banks may not lend on real estate (State banks may,) but they may secure previous *bona fide* loans by taking mortgages on real estate.

The reason for this regulation is that real property is not a good

banking security. A noted authority has said that anybody might conduct a bank if he would only learn the difference between a mortgage and a bill of exchange. First class bills are the banker's security par excellence.

5. Banks are limited to the following functions; the discounting of promissory notes, bills, drafts, and other evidences of debt; receiving deposits; dealing in exchange, coin, and bullion; lending on personal security, and the issue of bank notes.

6. After fully paying up their shares shareholders are liable for the debts of the bank to a further equal amount. No bank is permitted to establish branches.

7. The Secretary of the Treasury may deposit public money in a bank if the bank gives satisfactory security by the deposit of United States bonds "and otherwise." The last two words are important. United States bonds may not be available, then good municipal bonds may be substituted and failing these the personal bonds of the officers of the bank. The Secretary of the Treasury may thus exercise a very wide discretion in case of need. The most important regulations of the whole system now follow; they are the source of all the troubles of the United States commercial world with respect to the scarcity of money which is acutely felt at regularly recurring periods.

8. Banks having a capital exceeding $150,000 must deposit in the United States Treasury registered interest bearing bonds to an amount not less than $50,000.

Banks having a less capital than $150,000 must deposit bonds equal to 25 per cent of their capital. Each bank may then receive circulating notes known as National Bank notes to the amount of the market value of the bonds deposited, but the market value must not exceed the par value. At present the bonds are at a high premium, therefore the amount of notes in circulation is in all cases governed by the face value of the bonds. Of course the banks collect the interest on the bonds which remain their own property although in the possession of the Government.

The notes when received are in blank, merely certifying the fact that the security for them is in the hands of the Treasury; when signed by the officers of the bank they become promises to pay on demand, and may then be issued to the public.

Banks are not compelled to issue notes, and many of them do not, although they are compelled to deposit a portion of their capital with the Treasury.

There is a tax of one-half per cent upon the circulation of National Banks, and of 10 per cent upon the circulation of State and Private Banks. This, as was intended, has effectually extinguished the issue of notes of all institutions other than the National Banks. Notes for less than $5 may not be issued, and not more than one-third of those issued may be of $5. The total amount issued by any bank cannot exceed the paid-up capital.

The notes are receivable at par for all dues to the United States except duties on imports, and are payable for all debts owing by the Government within the United States, except interest on the public debt and in redemption of the national currency. Every bank must receive the notes of every other bank at par in payment of any debt due to itself; but they are not "legal tender" as between individuals.

9. *Redemption.*—Each bank must deposit with the Treasury of the United States "lawful money" (specie, or legal tender notes—greenbacks) to the amount of 5 per cent of its circulation as a fund for redeeming the same, but this does not cancel the obligation of paying on demand across

the counter. In case of default by any bank the Comptroller must declare the security forfeit, and give notice to note-holders to present their notes at the Treasury for payment in lawful money of the United States. Any gain from lost or destroyed notes goes to the Government.

Thus the Government guarantees the note-holder because it is itself a debtor of the bank. It promises to pay the note-holder who is a creditor of the bank instead of the bank itself. In practice the note is as good after the bank has failed as before, and continues on its course until it finds its way to the redemption bureau.

10. One-tenth of the net profits of a bank must be carried to the surplus fund until it is equal to 20 per cent of the capital. Banks must not lend more than one-tenth of their capital to any one person or corporation, nor may they lend upon security of their own shares. National Banks may not certify a cheque for a customer for more than stands to his credit at the time. (State Banks may over-certify.) Each bank must report to the Comptroller not less than five times a year in addition to special reports which may be called for at any time. The Comptroller is empowered to appoint examiners to make a thorough examination into the affairs of any bank.

11. *Reserves.*—We may consider the National Banks as being situated in towns or cities of three descriptions, viz. :—

(*a*) Ordinary towns or cities.

(*b*) Reserve cities, viz. Boston, Albany, New York, Brooklyn, Philadelphia, Pittsburg, Baltimore, Washington, New Orleans, Louisville, Cincinnati, Cleveland, Detroit, Indianapolis, Chicago, Milwaukee, St. Paul, Minneapolis, St. Louis, Kansas City, St. Joseph, Omaha, San Francisco, Savannah, Houston, Des Moines, Lincoln, and Portland. Any city of 50,000 inhabitants can be made a reserve city, upon application by three-fourths of the National Banks established therein.

(*c*) Central reserve cities, viz. New York, Chicago, and St. Louis. A city of 200,000 inhabitants may be made a central reserve city upon application by three-fourths of the National Banks established therein.

National Banks situated in ordinary towns (*a*) must keep a reserve equal to 15 per cent of their deposits. Banks situated in reserve cities (*b*) and (*c*) must keep a reserve equal to 25 per cent of their deposits. The reserve must in every case be "lawful money" of the United States, in other words, specie or legal tender notes—greenbacks. Clearing House certificates representing lawful money, and the cash reserve of 5 per cent, which every bank must deposit with the Treasury for redemption of circulation, may be also counted as part of the reserve against deposits. A bank in a reserve city may keep one-half of its reserve in the form of cash deposits in approved banks in a central reserve city. Similarly a bank outside the reserve cities may keep three-fifths of its reserve on deposit in certain approved banks in those cities.

It is a long-standing practice of these "reserve" banks to invite deposits from country banks by offering interest thereon. It can be well understood that this opportunity of converting a profitless reserve into an interest bearing item, which still counts as a reserve, is eagerly accepted. Thus there is a constant transfer of funds chiefly to New York, the banking metropolis of the country. The Bank of England holds the reserves of all the banks in the United Kingdom, and the "Associated Banks of New York" evidently occupy a similar position towards all the other banks of the Union as the chief depository of their reserves, the advantages and disadvantages of concentration being the same in both cases.

Certain penalties are provided for the breach of reserve regulations; thus, when the reserve of any bank falls below its legal limit it must be made good within 30 days, or a receiver may be appointed to wind up the affairs of the bank, but the Comptroller always uses this power with the greatest moderation. Again, until the reserve is restored the bank may not increase its liabilities by granting any new loans or discounts, except by the purchase of sight bills, nor may it declare any dividend. Here we have a hard and fast line which may not be passed, admirably calculated to increase any panic that may arise when money is gradually getting "tighter" on account of the surplus reserve gradually dwindling down to the statutory limit, and "no more loans" becomes the order of the day.

12. *Combined Reserves.*—In the management of every bank reserve there is a variety of conflicting interests. To avoid keeping idle cash investments in securities must be made, but the reserve must also be strong enough to inspire confidence in the public. On the approach of a time of trouble self-preservation prompts a contraction of loans and refusal of discounts, when everybody agrees that a liberal increase of accommodation is the best means calculated to allay the threatened danger. In the case of a single bank of vastly preponderating influence, as the Bank of England for example, a panic is much more easily controlled than in the case where there are several banks of equal influence standing side by side. The great difficulty is to get all to act together for the common good. There is always the contingency to be reckoned with that the timid ones will pursue a selfish course by reducing loans and increasing reserves, and leaving others to bear the heat and burden of satisfying public demands.

During the panic of November 1860 in New York the banks of that city invented and carried to a successful issue a plan of much merit. It has been tested several times since, and by other cities, with equal success, although it failed in September 1873 principally through tardy action. In order to secure unity of action the Clearing House Association was made the agent for carrying out the idea. The banks were already united through this institution, and no bank would willingly allow itself to be excluded from it. Accordingly the banks agreed that, in order to grant the usual accommodation to the public, the specie reserves held by them should be formed into a common fund, and if necessary should be equalised among the banks by levies made upon the stronger for the benefit of the weaker. For settling purposes a committee was appointed with power to issue certificates of deposit to any bank placing with them satisfactory security in the shape of stocks, bonds, or bills; and these certificates were to be received in payment by creditor banks. The effect of this arrangement was that if any bank experienced a disproportionate demand for specie it was supported by the whole of the central fund, while its debts to other banks could be discharged by pledging its securities. No bank had now any interest in accumulating and hoarding specie, since it would be held at the disposal of all as occasion required. The scheme is nothing more than a vast consolidation for mutual defence and support, and is usually called into operation when accepted by three-fourths of the banks in the association. In December 1895 when the Venezuela boundary affair caused a serious outflow of gold to Europe, arrangements were made in New York, Boston, and Philadelphia for the issue of Clearing House certificates if necessity arose.

The Silver Question.—The silver dollar as a legal tender coin was abolished by Act of Congress in 1873 after due discussion and deliberation. The production of silver in the United States has increased very much since

that date, but with the adoption of a gold standard by all the leading nations in recent years the market for the white metal has become correspondingly restricted. The silver party in the United States accordingly grew very clamorous for the reinstatement of the silver dollar —"the dollar of the fathers"—on equal terms with the gold dollar. The Congress of 1876 was elected to carry out this idea, and the result was seen in the Bland-Allison Bill of 1878. This measure directed the Government to purchase not less than $2,000,000, nor more than $4,000,000 worth of silver bullion monthly, and coin it into silver dollars of full legal tender. No less than $378,166,793 were coined, of which about $57,000,000 entered into circulation, the remainder being deposited in the Treasury by their owners, who received "Silver Certificates" for them (redeemable in silver) receivable for all public dues, but not legal tender. In 1886, 1890, and 1892 it was attempted to establish the "free coinage" of silver, but unsuccessfully. Stimulated by these public purchases the production of silver went on increasing until the output amounted to about 4½ million ounces monthly. The owners of silver mines and their friends were not slow to see the advantages that would accrue to them if the Government could be induced to take the whole quantity off their hands regularly. The Sherman Act of 1890 was passed, and the Government became the purchaser of 4½ million ounces of silver bullion monthly. Silver dollars which nobody wanted were to be coined at the rate of 2,000,000 ounces monthly until July 1891, when it was provided that coinage should cease and the bullion be stored in the Treasury. It was ordered that the metal purchased under this Act was to be paid for with Treasury notes which were to be redeemed on demand either in silver or gold coin at the discretion of the Secretary of the Treasury, the object being to maintain parity between the silver and the gold dollar, really for the first time in American history. The Treasury notes were declared to be legal tender in payment of all debts, public or private, except where otherwise expressly stipulated in the contract. On the closure of the Indian Mint to silver in 1893 the Sherman Act was immediately repealed, but not till 168,000,000 ounces of superfluous silver had been purchased.

UNITED STATES CURRENCY.—This is of a very diverse character and consists of—

1. *Gold Dollars.*—The Act of 14th March 1900 says, "The dollar of 25·8 grains of gold $\frac{9}{10}$ fine shall be the standard unit of value, and all forms of money issued or coined by the United States shall be maintained at a parity of value with this standard." The sovereign contains 123·27447 grains of gold $\frac{11}{12}$ fine. The Mint par between the United States and the United Kingdom is thus £1 = $4·86⅔ or $1 = 49 $\frac{5}{6}$ pence.

2. *Silver Dollars.*—The silver dollar contains 412½ grains of silver $\frac{9}{10}$ fine, and with silver at two shillings per ounce is worth about 1s. 8d. They are legal tender to any amount.

3. *Gold Certificates.*—Issued by the Treasury against deposits of gold coin. They are mostly of large denominations, none under $20, and are chiefly used by bankers.

4. *Silver Certificates.*—Issued against deposits of silver coin under the Act of 1878, and redeemable in silver dollars. In order to encourage their use they are now issued for sums of $10 and under. They are receivable for all public dues, but are not legal tender.

5. *Treasury Notes.*—Issued in payment of the silver purchases under the Sherman Act of 1890. They are legal tender for all debts, both public and private, except where otherwise agreed upon. They are redeemable in

gold or silver, but practically the Government binds itself to pay gold if required.

6. *United States Notes, or Legal Tender Notes, or "Greenbacks."*—Issued by the Treasury in 1862-63. Their amount is limited to $346,681,016. They are secured by a special gold reserve of $150,000,000, and are legal tender to any amount. Like the Bank of England note, they are redeemable in gold on demand at the Treasury, or any sub-treasury of the United States.

7. *National Bank Notes.*—Issued by the National Banks, and secured by a deposit of United States bonds with the Treasury. They are redeemable at the various banks in either greenbacks or gold, therefore although they have never been legal tender as between individuals they are as good as gold.

Although the various classes of currency enumerated above have been issued under more or less varied conditions and limitations, they are all as good as gold in the United States, but the banking student will bear in mind that for international purposes silver dollars and their paper representatives are useless; gold is the only standard.

MODERN CONDITIONS.—The commercial history of the United States shows that from the earliest colonial times, when wampum beads and tobacco certificates were "lawful money," down to the present moment there has been one continuous struggle for a sufficient and self-regulating currency, and the struggle must under present conditions go on. The American people have always shown a decided preference for paper money. The issue of greenbacks is strictly limited and cannot be increased, therefore it is to the National Banks and the National Bank note that the commercial world must turn for relief. National Bank notes can only be obtained by depositing United States bonds, representing the national debt, and if the price of these bonds stands at a high premium, it is difficult to see the advantage of depositing a $140 bond in order to be allowed to circulate $100 in notes. The Currency Act of 1900 sought to rectify this incongruity, and provided that certain outstanding bonds, all redeemable before 1909, might be converted into 2 per cents which should not be redeemable for thirty years. Other steps were also taken, and the circulation of National notes was raised considerably, amounting to a total of over $324,000,000 at the end of 1902. On account of the low interest, together with the tax of one-half per cent, it is not surprising that banks are not particularly anxious to keep up a large circulation. Again, the demand for notes varies with the condition of trade. But if a bank takes out extra circulation in the busy portion of the year, when money is in request, it cannot retire its surplus at will when the dull season comes. The law provides that only an aggregate of $3,000,000 may be retired monthly, this being effected by depositing lawful money to an equal amount in the Treasury. In times of great prosperity, when currency is urgently needed, bonds are often unpurchasable. Either the price is prohibitive or they are simply not to be obtained. The bulk of United States bonds is held by insurance companies, trust companies, State banks, trustees, and private persons, who have made permanent investments therein and do not wish to realise. Thus the currency is rendered decidedly inelastic. During the stringency of the autumn of 1902 the Secretary of the Treasury actually circularised the principal New York banks to get them to take out more circulation. Bonds were even begged and borrowed for deposit with the Treasury, and bonds of first-class municipalities were likewise accepted (with a good margin), so

necessary had it become to do something for the relief of the money market.

The United States Government does not keep a banker, but all taxes and duties are paid into the Treasury direct, and there they remain, as useless to the commercial world as if they had been sunk at the bottom of the sea. While on their way the Secretary has power to deposit them in certain banks, but once the money actually reaches the Treasury it is a most difficult matter to get it out. The Secretary has then no power to grant loans or transfer funds to a bank. Customs duties on imports are payable in legal tender, and must be paid into the Treasury or various sub-treasuries direct. It can well be imagined what an amount of cash is thus withdrawn from the market by the port of New York alone. In the first quarter of 1900 no less than 84·5 per cent were paid in gold. In the case of our own fiscal system the taxes stream into the Bank of England for the Government account, and are returned into the channels of trade in an equally brisk stream. This can be done because the Bank of England is the Government banker, and your banker will do just as he pleases with your money once it is deposited with him. The only methods by which money can be got out of the United States Treasury are as follows:—

1. By defraying ordinary expenditure.
2. By prepayment of interest on bonds, at a rebate.
3. By purchasing bonds, that is, paying off a portion of the national debt.

When it becomes known that the Secretary of the Treasury is a purchaser, it is at once surmised that he is practically compelled to buy in order to relieve his bursting coffers. The price is accordingly put up against him, and possibly he cannot obtain bonds at all. But in any case the purchase of bonds must reduce the amount available as security for National notes, and an inquisitive person might ask what would happen if the national debt could be paid off suddenly? Well, there would be an end of National Bank notes, and as time is the one certain element governing the life of the national debt, so surely will its lapse bring the present note system to an end—if nothing be done; but, of course, before thirty years run off some more tinkering will be done, but no amount of tinkering at the present system can render it permanent and self-regulating. Moreover, if the present system is continued, then it appears that in order to provide a currency, and an unsatisfactory one too, the people of the United States are to be compelled to go on paying interest upon a national debt which they could easily extinguish.

It sounds very strange, but it is nevertheless true, that if a bank manager went to the Treasury with "a king's ransom" in gold as security, he would not be granted a single $5 note. We must not, however, conclude that there is no market for gold in the United States; on the contrary, gold bullion is received at any mint or assay office, and is paid for within two days at the rate of $20·67 per fine (pure) ounce. As a matter of fact the Treasury holds the real gold reserve of the country, and whenever any large quantity is required, no matter for what purpose, it is the Treasury which supplies it.

The strain upon the Associated Banks of New York always comes in autumn. The reason is not far to seek, and is found in "the moving of the crops." The reaping of the wheat fields of the north and west, and the ingathering of the cotton of the south, alike demand money and plenty of it. The labourer must be paid in currency; if a regular hand, his wages have probably been accumulating for months, and pay day is now at hand.

Retail business is also brisk, the shopkeeper must keep more cash in his till, and accordingly pays a visit to the local bank, his banker probably draws on his reserve, which is partly deposited with a reserve bank, and the reserve bank passes on the call to New York. Possibly the farmer has already "drawn" against his crop, and his acceptances are now maturing.

Let us look a little more closely into some of these commercial transactions and see what important services banking renders to trade. For example, how does the United States obtain payment for the immense quantities of cotton which it exports annually to this country? "To explain this properly we shall have to go back to the beginning of the transaction. We must presuppose that a Liverpool house importing cotton is represented in one of the cotton centres in the States, say Galveston. In a place of that kind there will be, when purchases have to be made, a partner or agent of the Liverpool house which wants to import the cotton. In dealing with exports the main thing, both from the exporting and banking point of view, is to get the goods represented by some kind of document. Until they are so represented the banker cannot deal with them. The first object, then, of the man in the States who buys on behalf of his partners or employers in Liverpool is to get the cotton put on a truck at the nearest railway station, and obtain a through bill of lading for it from the company. Directly he gets this document he is able to go ahead. He draws, say, on a Liverpool bank by arrangement, attaching to the draft the bill of lading and other documents—copy of invoice, insurance certificate, etc.

"He then goes to the local banker, to whom he gives a letter of hypothecation over the cotton, and the banker gives him cash which will enable him to continue operations.

"The Galveston bank forwards the bill of exchange and the attached documents to its agent in London or Liverpool. The agent presents the bill for acceptance to the bank in Liverpool on which it is drawn. The Liverpool bank accepts it 'payable in London,' retaining the documents against its acceptance. This is reasonable. The bank, by accepting, has made itself liable for payment of the bill at maturity, and requires a set-off of some kind. This is represented by the documents for the cotton, and if the bill should not be paid at maturity the bank is able to sell the goods. Meanwhile the cotton arrives, but the firm to whom it has been consigned cannot get possession of it until it gets possession of the shipping documents, these being, as we have seen, in the possession of the bankers, held against their acceptance. If it be a broker who applies for the documents, the bank gives them up to him on his signing an undertaking to do one of two things. He undertakes that if the cotton is not sold, it shall be stored in the name of the bank in an independent warehouse, but that if, on the other hand, the cotton is sold, the proceeds shall be duly handed to the bank within the customary period—ten days. It is the business of the customer in this transaction to see to the insurance; the letter of hypothecation which the bank takes from the broker states for how much and with whom the insurance has been effected. This, in rough and general outline, is how our cotton imports are financed."—F. E. Steele in the *Bankers' Magazine*, March 1902.

There is another source of anxiety for the Associated Banks which has made itself felt very recently. The Loan and Trust Companies compete with the banks at various points; they receive deposits, collect accounts and do banking business in a large measure, but do not hold any reserves although many of them possess the privilege of membership of the Clearing

Association. It is argued that by not holding reserves they are a standing menace to their neighbours. They increase the danger of panics, and when a panic comes they are quite unable to assist in allaying it. The Clearing Association has now called upon the Trusts to keep a reserve of at least 5 per cent of their deposits, to be gradually increased to 10 per cent. Several of them have refused to accede to this demand, preferring to sever their connection with the Association; other secessions are anticipated, but it is difficult to see what harm will result to the "Clearing" by this action.

Below we give the weekly return of the Associated Banks of New York for 27th June 1903 as published by the *Financial News*. It is worthy of a moment's study.

	June 27.	June 20.	Increase or Decrease.
Loans and discounts	$913,750,000	$904,820,000	+$8,930,000
Specie	163,770,000	158,460,000	+ 5,310,000
Legal tenders	75,080,000	74,085,000	+ 995,000
Net deposits	903,720,000	889,780,000	+13,940,000
Circulation	44,090,000	44,009,000	+ 81,000
Reserve held	$238,850,000	$232,545,000	+$6,305,000
Legal reserve	225,930,000	222,445,000	+ 3,485,000
Surplus reserve	$12,920,000	$10,100,000	+$2,820,000

Compare the 75 millions of "Legal tenders" (principally greenbacks) with the 44 millions of "Circulation"—National Bank notes. We must recollect that the latter were originally intended to supersede the former, but verily, as Mr. Knox pointed out years ago, "the Legal tender note has risen up and strangled the National note at every turn." Next notice the amount of the "Legal Reserve," which, according to law, must be 25 per cent of the "net deposits." Divide $903,720,000 by 4, and we obtain $225,930,000 as given. But the actual "Reserve held" shows an excess of "Surplus Reserve" of $12,920,000 over and above the Legal Reserve. It is this item which is anxiously scanned by the United States business man; the closer the two sets of figures approach each other the tighter does money become and the higher rates. It must be borne in mind, however, that when we hear of rates of 20 per cent and upwards, it is the brokers and trusts who get them, not the banks; they seldom get more than 6 per cent, their legal figure.

The return for the week ended 20th September 1902 showed that this surplus reserve had not only vanished, but was represented by a deficit of over $1\frac{1}{2}$ million dollars. This does not mean that *all* the Associated Banks were deficient in the matter of reserves, but it does mean that in the aggregate they had broken the law, and that a great many of them automatically ceased granting loans and discounts. Now here comes the irony of the situation. The banks, although below the minimum, held an actual reserve of over 44 millions sterling as compared with the Bank of England reserve, for the same week, of $26\frac{1}{2}$ millions sterling. That is, the New York banks held nearly 18 millions sterling more than the Bank of England, and were forbidden to go on lending and discounting, while the Bank of England calmly went on financing the British Empire, which, in the words of an ancient mathematician, "is absurd." Evidently there must be something wrong with a system which does not permit of such an abundance of money being used in a legitimate manner. Here is the spectacle of a country, rich in capital and resources of every kind, which

studiously deprives itself of the means of conducting its business with ease and comfort. There are indications that its statesmen are at last awake to their country's needs, and that legislation on the subject cannot be long delayed.

Banking in Germany

Previous to the establishment of the German Empire in 1871 the various members of the Confederation had each its own system of banking. As regards coinage some used the thaler system, while others adopted the gulden, but in the aggregate there was a mass of old and worn coin in circulation, mostly of obsolete denominations. All the States—with the exception of the free city of Bremen, whose standard of value was gold—adhered to the silver standard. There was a limited number of gold coins in circulation, composed of such diverse pieces as Frederics d'or, ducats, crowns, napoleons, pistoles, eagles, and Russian imperials. It was on account of having to settle in the course of international trade that such a heterogeneous mass of coin was able to be used, silver alone being useless for such a purpose. Every member of the Confederation, with the exception of the three free cities and the principality of Lippe, issued paper money to suit its needs. There were also thirty-three banks of issue established according to the ideas of the state or town in which they existed. Some of these held charters revocable at pleasure, others held them for a term, while the remainder held theirs in perpetuity. The amounts of their authorised issues varied considerably, as also did the regulations governing their reserves.

To reduce this chaos to order was the problem which taxed the ingenuity of German statesmen for the first four or five years of the newly-fledged Empire. It was fully recognised that it was useless to expect the Empire to make that progress which its laboriously acquired unity was calculated to achieve until unity in banking and currency had been established. The adoption of the gold standard by the Act of July 1873 was the first step towards this consummation. Some say that this step was taken on account of German hatred to everything French, including their bimetallic system. Others say that it was purely imperialist ambition which it was now possible to gratify with the help of the five milliards of war indemnity, while yet others say that it was because the prosperity and wealth of England have been attributed in the main to her gold standard, and therefore it must be a good thing for the other nations to adopt. The law of April 1874 swiftly followed. It provided for the extinction of the paper money issued by the various States by creating a currency of Imperial Treasury notes, or *Reichskassenscheine*, issued in denominations of 5, 20, and 50 marks, redeemable in gold on demand at the Treasury, but not made legal tender. It also provided for the issue of Imperial paper, the result being that twenty local issues were extinguished, amounting to 180,000,000 marks.

The ground being thus prepared, it only remained to establish a new Imperial State Bank which should control the note issue and maintain the standard of value on a gold basis throughout the Empire. The bank was to be under direct Imperial supervision, as were also the other banks for the future, while a new set of regulations was to be formulated for the whole. The Act of 1875 performed all this. As regards the new central bank it was already at hand in the shape of the Bank of Prussia. Established in 1765 by King Frederick II. of Prussia, it was already a State Bank, its original capital of 2,000,000 thalers being supplied by the State. Private

stockholders were admitted in 1847, its capital was increased to 20,000,000 thalers, and notes were issued, but the State still retained its original control and the lion's share of the profits.

It was under these circumstances that the Bank of Prussia was raised to the dignity of the Bank of the Empire, or *Reichsbank*. As the Royal Bank of Prussia it ceased operations on 31st December 1875. From being the financial institution of a comparatively restricted country it has become one of the most noted banks of Europe, its functions being to regulate the money circulation of the German Empire, to facilitate settlements, and utilise available capital.

The main clauses of the German Bank Act of 1875 are:—

1. The right of issue is now only to be obtained under Imperial sanction.

2. There is no obligation to accept bank notes in case of those payments to be legally discharged in coin.

This, however, has not hindered the circulation of Imperial Bank notes.

3. Bank notes are issued in denominations of 100, 200, 500, and 1000 marks.

4. Every bank must redeem its notes on presentation. Damaged notes are made good by the bank, but it is not obliged to indemnify for lost or destroyed notes.

5. The Imperial Bank must pay its notes in current German money in Berlin. It may also pay at its branches if circumstances permit.

6. The Imperial Bank must exchange its notes for gold bullion at the rate of 1392 marks for one pound (500 grammes) fine (pure).

Tests are conducted at the expense of the seller.

7. Banks of issue are not permitted to accept bills, or buy or sell merchandise or current commercial paper on credit.

8. Banks of issue must report to the proper authorities four times per month.

9. Banks whose note circulation exceeds the coin reserve and amount of notes prescribed in proportion to capital must pay a tax of 5 per cent per annum on the excess to the Imperial Exchequer. The Imperial Bank is empowered to issue notes in proportion to its business needs.

This is the famous German "elastic limit" of which so much is heard in connection with discussions on bank reserves.

10. The Imperial Bank is required to maintain a money and bullion reserve equal to one-third of its notes in circulation. This reserve may include German currency, Imperial Treasury bills, and gold bullion or foreign gold coin valued at 1392 marks per pound (German) fine.

The remainder of the notes must be protected by discounted bills having not more than three months to run, and usually protected by three, but never less than two, solid accredited vouchers.

11. The Imperial Bank and its branches are free from all revenue or State taxes throughout the Empire.

12. The Imperial Bank is authorised to buy or sell gold and silver coin or bullion; to discount, buy, or sell inland or foreign bills of exchange which have not more than three months to run; and to discount, buy, or sell bonds of the Empire or any German State, provided that they will mature in not more than three months.

13. No advances are made to foreigners. Only persons of known good character are granted accommodation, the time limit being three months.

The Bank may transact Lombard or deposit loan business, on gold or

silver, coined or uncoined, or on interest-bearing bonds of the Empire, or any state or municipal corporation.

Foreign bonds to bearer, railway shares and debentures, merchandise lying in a warehouse in the country, and several other descriptions of property, are accepted as security for loans, but in every case an appropriate margin is deducted.

14. The capital of the Imperial Bank is (now) fixed at 180,000,000 marks, and the shareholders are not personally responsible for the obligations of the Bank. The profits of the Imperial Bank are divided between the shareholders and the Government. The charter of the Bank is renewed every ten years, and the Government has always the option of taking over the whole concern at a valuation.

The renewal of the charter is usually the occasion of some fresh concession by the Bank.

At present the shareholders take a first division of 3½ per cent on their capital, then 20 per cent of the remainder of the profits. The Government takes 60 per cent of the same, and the remaining 20 per cent goes to the rest or surplus until it reaches a sum of 60,000,000 marks. When this amount has been accumulated the shareholders will take 3½ per cent as their first dividend, and 25 per cent of the balance remaining, the State's share being increased to 75 per cent.

15. The Bank is supervised by an Imperial Board composed of the Chancellor of the Empire as president, a member appointed by the Emperor, and three other members appointed by the Federal Council. The directors of the Bank are appointed for life, but are subject to the Imperial Chancellor. The shareholders exercise their part in the government of the Bank through their General Assembly, from which a Central Committee is elected. Many details are remitted to this committee, such as the examination of weekly reports, the inspection of deposit accounts, the amount of loans to be granted and paper to be purchased, the rate of discount to be charged, and arrangements with other banks.

The Act has regulated the note issues very carefully. Previous to the foundation of the Empire it was the constant aim of the thirty odd issuing banks to put as many notes as possible into circulation, and a large proportion of this paper consisted of notes for very small sums, as low as one thaler (three shillings). From 1876 onwards notes for less than 100 marks (say £5) have been forbidden.

The note issue of the Reichsbank was largely modelled upon that of the Bank of England, while certain weak points were at the same time carefully avoided. Thus both banks are authorised to issue a certain amount of uncovered circulation, the former at the present time 470,000,000 marks, the latter £18,450,000. As is well known, gold must be deposited to the amount of its face value for every extra note issued by the Bank of England. It takes an Act of Parliament to relieve the Bank from this regulation. The Reichsbank likewise must hold cash against all notes issued beyond its fixed amount, but here comes the "elastic limit." It may go on issuing notes uncovered by cash, but must pay a tax of 5 per cent per annum on the excess. In any case, however, it must hold cash against one-third of its total circulation. The limits of the fiduciary issue have been frequently overstepped, and sometimes for protracted periods, but the metallic reserve has been at least 70 per cent all the time. The notes have been issued almost unnoticed, and have returned as quietly, in contradistinction to the hard and fast line drawn by our Act of 1844, which has had to be suspended on no less than three well-known occasions.

Of course the tax of 5 per cent is the practical cure for these excess issues. At such a time, if the Bank does not raise its rate to a similar amount, it must be a loser, and cannot afford to continue such a course for long, while, on the other hand, if it raises its rate so as to cover itself, or still make a profit, borrowers are discouraged. Thus both sets of circumstances tend to restore a normal condition of affairs. As an aid to checking a drain of gold, the other banks of issue must not discount at a lower rate when the Reichsbank is charging 4 per cent or more. Under other circumstances they may only quote at one-quarter below the Bank.

The following is taken from the *Daily Telegraph* of 18th August 1903:—

"The return of the Imperial Bank of Germany for the week ending the 15th inst. shows the following changes as compared with the previous account (taking the exchange at 20 marks to the pound):—

	Amount.	Increase.	Decrease.
Cash in hand . .	£47,501,950	£1,191,850	
Treasury notes . .	1,429,700	54,100	
Notes on other banks .	711,550	212,300	
Other securities . .	39,432,700	...	£405,950
Advances on stocks .	2,954,150	187,150	
Sundry securities . .	93,350	6,800	
Sundry debtors . .	4,047,200	...	55,800
Notes in circulation .	58,137,600	...	1,270,900
Bills and public deposits	26,911,750	2,431,858	
Sundry creditors . .	1,241,900	29,500	

"Note circulation below the legal maximum (free of taxation) £15,005,600, against £12,276,450 below the legal maximum last week."

To find the amount of note circulation below the legal maximum we proceed thus:—

Add together "Cash in hand," "Treasury Notes," and "Notes on other banks," as given above, total £49,643,200, which "covers" notes to an equal amount.

Subtract this total from "Notes in Circulation"; the difference is £8,494,400, which represents the actual "uncovered" issue.

But the legal maximum of uncovered issue is £23,500,000 (470,000,000 marks); therefore the Bank might issue a further amount of £15,005,600 free of taxation, as stated above.

The use of notes and specie is much greater in the German commercial world than with us. In this country the cheque performs most of the work. The Reichsbank aims at rectifying this, and has accordingly greatly developed its system of current accounts (*Giro-Verkehr*). The idea is to enable persons in different parts of the Empire to settle without having recourse to currency. For example, a debtor in a distant city may settle with his creditor in Berlin by paying in the amount of his debt at the branch of the Reichsbank in his city, and on the following day his creditor's account at the head institution in Berlin is duly credited. There is no charge for the transfer, and the debtor need not have an account with the Bank. Naturally the most important business of the Bank is the discounting of bills, about 80 per cent of its profits being derived from this source. By far the greater portion are inland bills. In the balance sheet for 31st December 1900 bills drawn on England stood at £3,734,120, and bills on other foreign places at £39,159. Why is there such a decided preference for bills on this country? Because London is the one great free

market for gold. A bill drawn on London is payable in gold. There is no uncertainty about it, and the bills in question mean the ability to draw nearly $3\frac{3}{4}$ millions in gold from us if necessary, also the ability to check any tendency towards an outflow of gold from Berlin.

In the case of bills drawn on Paris or Berlin it would be possible to pay the former in silver five-franc pieces, and the latter in silver thalers. The *right* to do so exists. Strangely enough, the officials of the Bank of France and of the Reichsbank respectively always protest loudly when reminded of this fact. Rightly or wrongly, the latter institution has always been accused of putting obstacles in the way of any person unpatriotic enough to desire to pay his foreign creditors with German gold. He usually does so "at his peril." At the Brussels Monetary Conference of 1892 the German representatives affirmed that the Reichsbank had never paid any one in silver who demanded gold, and had never made any difficulties about paying gold, whether it was wanted for export or not. One delegate said that if the Bank should refuse to pay gold the Government would immediately put it into liquidation. The old thalers are gradually being absorbed by the German mint. According to German mint law $69\frac{3}{4}$ twenty-mark pieces must contain 500 grammes of pure gold. Our sovereign contains 7·98805 grammes of standard gold ($\frac{11}{12}$ fine), hence the mint par between the two countries is £1 = 20·429 marks, usually called 20·43. With the exchange standing at 20·33 gold usually leaves us for Germany, while London always draws gold from Berlin at 20·53. The Reichsbank will smooth the way for an importation of gold by granting a six-day loan free of interest if repayment is promised in gold. Thus a shipper loses no interest while his consignment is in transit. Moreover, the Bank is more lenient to the seller than the Bank of England in its assay of foreign gold.

The Imperial Bank has endeavoured to assist farmers and small tradesmen as far as possible, but not to their entire satisfaction. The Bank is of course not intended to afford long credits, but customers with sound commercial reputations are always suitably accommodated. It is not everybody that is so fortunate, and to suit this latter class have arisen those associations originated by Dr. Schulze of Delitzsch. The institutions, known as *Volksbanks*, have also spread to Italy, where the *Banca del popolo* is equally appreciated. They are conducted under mutual principles, are self-supporting, and do a savings bank business as well. They afford accommodation to the small trader and others who are often in need of a loan, but are unable to obtain the usual facilities. A *Volksbank* is formed by a number of members, who take a share each and pay an entrance fee. The share is paid up by regular periodical instalments. All payments and fees are very small, and no member can hold more than one share. Deposits which bear interest are received both from members and outsiders. Thus the loan fund is built up of the shares paid by instalments, the deposits, and savings. A shareholder can obtain a loan up to the amount of his share, but for anything above that amount he must deposit security or provide a surety. Only shareholders may obtain loans. The classes who make most use of these banks are the well-to-do artisans, shopkeepers, and small traders, to whom it is a convenience to be able to keep a banking account, and cheque-books are accordingly supplied.

There are some 6000 joint-stock banks in Germany, many of them large and powerful institutions. They are all subject to the Act of 1875, and their operations are similar to those of the Reichsbank. Some of the richest and most enterprising, such as the Deutsche Bank and the Dresdner Bank,

have established branches in London in order to compete with us upon our own ground. The Deutsche Bank is probably the most noted of these. It has a capital of 7½ millions sterling and a balance sheet with "sides" of 50 millions. It is little wonder that with its careful management it is rapidly becoming one of the richest and best foreign banks in London, able to pick and choose its business, and came through the German trade depression of 1900-1901 with a greatly enhanced reputation.

Within recent years London has experienced quite an invasion of foreign bankers fully determined to wrest a large share of business from our countrymen. Many of our banks do a large foreign business, but it goes through the hands of agents. Thus there are two profits to be made. In former years exchange business was simply handed over to a broker. This had to be altered with the coming of the foreign banker, who is not slow to point out the advantages of placing commissions with his house, and the corresponding saving effected.

Banking in France

John Law of Lauriston, the famous Scotsman, established the first bank of issue in France in 1716. In 1718 it became the Government bank under the name of the Banque Royale, but its paper was issued at such a rapid rate that it soon stopped payment. The second bank of issue, thanks to the lesson learnt from Law and his disastrous schemes, was not established until 1776. The Caisse d'Escompte du Commerce (Bank of Commercial Discount), as it was called, owing to the interference of the Revolutionary Government, was suppressed by the decree of August 1793. Then followed the tide of *assignats*, which, in September 1796, amounted to 45½ thousand millions of francs, and were worth one-thousandth part of their face value. When these and their successors, the *mandats territoriaux*, had disappeared credit began to flourish again. The issue of notes now needed no authorisation, and several banks were opened.

When Napoleon came upon the scene he soon found the need of banking facilities and assistance, and following the counsel of his financial advisers the Bank of France was founded in January 1800, with a capital of 30,000,000 francs, in shares of 1000 francs each. To show the public a good example Napoleon himself, his family, and friends took shares.

Its scope of operations was as follows:—

1. To discount bills of exchange and drafts to order bearing signatures of at least three French citizens or foreign merchants of acknowledged reputation and solvency.

2. To undertake collections for the account of private citizens and public establishments, and to make advances in cases of such collections as may appear to be secure.

3. To receive on account cash deposits and collections on behalf of private citizens and public establishments.

4. To issue notes payable to bearer at sight, and notes to order payable within a certain number of days after sight. These notes as issued by the Bank to be so proportioned to the reserve cash in the vaults of the Bank, and with such regard for the maturing of negotiable paper held by the Bank, that the Bank can at no time be exposed to danger of delaying payment of its obligations when presented.

5. To open a bank for investments and savings wherein all sums offered in excess of 50 francs should be received for repayment at stated periods.

All transactions other than in gold or silver were prohibited, and with the exception of the last clause respecting investments and savings the original regulations are still in existence.

In 1803 the Bank was endowed with the exclusive power of issue in Paris, and its capital was raised to 45,000,000 francs, but the Government reserved the right to permit banks of issue outside Paris. From time to time nine banks were permitted in various parts of France, but in 1848 they were all consolidated with the Bank of France, which has remained the sole bank of issue in France to this day. In 1806 the capital of the Bank was raised to 90,000,000 francs, and though becoming still more intimately connected with the Government it remained a public institution. The direction of the Bank was entrusted to a governor and two sub-governors appointed by the chief of the State, but paid by the Bank; thus although a private corporation it became a State engine of a very important kind, and has continued to be so.

Although authorised in 1808 to establish branches (*comptoirs d'escompte*) very few were opened, and these were closed by the Bourbons in 1817-1818, and independent banks with the right of issue substituted. Next the Bank was authorised to establish fifteen branches in the chief cities with the sole right of issue in those cities, but the whole business was pursued in a half-hearted manner. To rectify the confusion which prevailed the Government converted the nine independent banks which existed into branches of the Bank of France, and at the same time the capital of the Bank of France, which had been reduced, was raised to 91,250,000 francs.

The Bank of France, throughout its whole career, has evinced a marked reluctance to establish branches. The Bank of England has been criticised for taking a similar course, but our own banking system having been highly developed from an early period England has not suffered so much from such a deficiency as her neighbour. Napoleon III. called upon the Bank to establish a branch in every department (territorial division) within ten years. By 1869 65 were in operation, but the full number was not completed until 1882. Various additions have been made to the number since then, and there are now 126 branches, 49 auxiliary offices, and 218 towns connected with the Bank.

A branch of the Bank of France is provided with a certain amount of capital, and does business under the supervision of the head institution, having few or no transactions with other branches. The manager is appointed by the Government and is assisted by a staff from Paris. The directors are chosen from a list made up in Paris, but sometimes partly by shareholders on the spot. The greater part of the discount business of the Bank is done by the branches, thus justifying their existence, but this was not so from 1814 onwards: the revolution of 1848 ruined most of the discount houses in the capital, and in the country the smaller commercial people suffered so much from lack of banking facilities that the Government had to step in and establish a temporary remedy. Public and private money combined provided the necessary capital, and discount offices were founded in Paris and throughout the country. They soon began to do a greater amount of business than the Bank of France, and some were eventually reconstructed as banks of discount after repaying the State its original portion of capital. The Comptoir d'Escompte de Paris was one of these; it came to grief in 1889 through being associated with the copper syndicate, and was then resuscitated with the encouragement of the Government, under the title of the Comptoir National d'Escompte de Paris.

It has a paid-up capital of £6,000,000, and now stands in the front rank of French financial houses.

The Bank of France suspended specie payments in 1848, and for the next three or four years had a very anxious time, which was followed by a period of such prosperity that in 1857 it was found convenient to double its capital to its present figure of 182,000,000 francs, and to extend its charter to 1897.

The period 1870-4 was the most critical in the Bank's history, embracing as it did the war with Germany, the struggle with the Commune, and the payment of 5 milliards (5,000,000,000 francs) war indemnity. Although its fate at one time hung in the balance, yet in the end patriotism, combined with superb finance and good management, carried it triumphantly through. The war broke out in July 1870, and on August 12 the Bank was authorised to refuse to pay cash for its notes, which were made legal tender, and the issue limited to 1,800,000,000 francs.

Two days later it was found that if the Bank was to afford its usual accommodation the limit must be raised to 2,400,000,000, and this was done. Notes for 25 francs were also authorised. On 13th August it was decreed that payment of all commercial debts should be postponed for one month. This period was extended from time to time until July 1871—the debtor being liable for interest up to the settling day. Specie payments were resumed in 1877.

By July 1871 the Bank had advanced to the Government 1,425,000,000 francs, and to the city of Paris 210,000,000 francs.

The greatest danger that ever beset the Bank was the probability of being plundered by the Communists, who were appeased in the early part of 1871 by being allowed to withdraw a sum of 9,400,000 francs standing to the credit of the city. After setting fire to the Tuileries they demanded 700,000 more to pay their men, and obtained it by threatening to seize the Bank. Next day the regular army appeared upon the scene and further danger was averted.

The next task of the Bank was to arrange for the payment of the war indemnity. According to the terms of the treaty, 500 millions of francs were to be paid one month after order was restored in Paris, 1000 millions by the end of 1871, 500 millions on 1st May 1872, and 3000 millions on 2nd March 1874. When the French Government set about obtaining this vast sum, it was found that, thanks to the credit which France enjoyed abroad, and the "old stockings" of her thrifty people, over eight times the necessary amount could be obtained. Thereupon President Thiers determined to liberate the soil of France at the earliest possible moment, and this was consummated by the payment of the final balance in August 1873, to the great chagrin of the conquerors, who were sorry they had not asked for more. This was effected by the Government buying bills drawn by Frenchmen upon their debtors everywhere. British bills were in great request, and specially acceptable to the German Government, because of their power to draw gold from the Bank of England. A Frenchman who bought some of the public loan, and paid for it with his draft upon England, simply exchanged his claim upon his English debtor for one upon his own Government.

THE LATIN MONETARY UNION.—This was a convention formed in 1865 between France, Belgium, Switzerland, and Italy for the purpose of supporting the "Double Standard," by which gold and silver ranked on equal terms in all business payments.

These countries agreed to make their coins of the same fineness,

diameter, weight, and current value, and to accept them indiscriminately as legal tender. Hence the francs and centimes of France, Belgium, and Switzerland, and the lire and centisimi of Italy, differ only in their mint impression.

According to French mint law 155 napoleons (gold 20-franc pieces) $\frac{9}{10}$ fine weigh 1 kilo. This gives a mint par with this country of £1 = 25·2215 francs. The silver 5-franc piece weighs 25 grammes.

Shortly afterwards Greece entered the convention, and the same system has been adopted by Spain, Servia, Bulgaria, and Roumania, although they have not joined the Union.

For a long time previous to 1871 the market ratio of gold to silver was 1 : 15½, but the greatly increased output of the silver mines, together with the large sales by Germany on her adoption of the gold standard in 1873, completely broke down this ratio, and silver became by far the cheaper metal.

The consequence was the Latin states quickly found themselves being drained of gold and inundated with silver; therefore, in 1876, their mints were closed to the free coinage of the latter metal. France, however, retains the right to pay her debtors in silver 5-franc pieces or in gold at discretion. The coinage of silver 5-franc pieces has been suspended since 1878. It is said, however, that it is really impossible to do without this coin, as it is the coin of the country people. The 5-franc gold piece is too light, and the note is too flimsy.

Thanks to the limitation of silver coinage and the consequent protection against over-supply the standard is easily maintained.

This ability of the Bank of France to use silver at par does away with the necessity of raising the discount rate like the Bank of England. Since it may redeem notes and pay debts in silver, it therefore simply charges a premium for the delivery of gold. The Bank officials say that it is only the bullion dealers and those who desire to make a profit who have to pay, but a change in the discount rate would also hit the merchant and the trader whose transactions are in notes or credit. Still the Bank dare not maintain a high or permanent premium, because this would simply proclaim the fact that its paper was inferior to gold. It is seldom that the metal can be obtained in sufficient quantity for export, and recourse is therefore had to the bullion dealers, who buy the coin from railway companies and big traders at a small premium. The circulation suffers accordingly, and the loss must, in the end, be made up at the Bank's expense.

At present the Bank of France holds not less than £100,000,000 in gold and £45,000,000 in silver, the circulation being in the neighbourhood of £170,000,000. The maximum circulation permitted is 5,000,000,000 francs.

It is worthy of notice that the Bank of England, the Bank of France, the Imperial Bank of Germany, and other big institutions of the same character, although they act as State bankers, are not State banks, but private concerns, none of the capital being held by the various Governments.

In the case of the Bank of England this is pure accident, in other cases it is deliberate design; for had the Bank of France been State property, as is the Bank of Russia, when the Germans entered Paris in 1871 they would have been justified in seizing the Bank of France and its treasure as lawful spoils of war; but being private property it was respected as such.

Operations of the Bank of France.—These consist of services which are obtainable by certain persons only, and others which are obtainable by the public at large. Open accounts are granted to private persons and public institutions, but all sums are received without interest. Some of

these accounts carry the privilege of discounting paper, and funds deposited may be drawn upon by drafts payable in Paris or at the various branches or subsidiary offices. Bills may be made payable at the Bank, and those presented by the Bank messengers may be paid by cheque or transfer.

Open discount accounts are allowed to persons who reside in a place where there is no branch or office of the Bank, and in this case all business is conducted by correspondence. All the advantages of residing in a bank place are therefore obtainable.

Loans against collateral are granted on State bonds up to 80 per cent, municipal bonds 75 per cent, and dividend-earning railway stock to 60 per cent. The minimum loan is 250 francs for not less than a fortnight or more than three months. The rates are from 1 to 1½ per cent higher than for discounts, in order to prevent borrowers from speculating in exchange as between the rate of the bank and exchange reports.

Safe deposits of all kinds are accepted, only trust fees being charged. The Bank also takes charge of foreign bonds, collects the interest, and watches for drawn bonds.

By an arrangement with the Russian Government, a holder of Russian public funds may deposit them without charge, and the certificate of deposit which the Bank grants is held valid for the value of the stocks deposited. This is designed to obviate the inconvenience resulting from Russian legislation on the subject of lost, destroyed, or stolen negotiable property, and is a public boon.

The writer was a party to a case in which Russian bonds of the 1862 loan, purchased in 1871, were immediately afterwards lost or destroyed. The loan was converted in 1889, and the Russian Government, after some persuasion, admitted the par value of the missing bonds, but required the holding to be increased by 15 per cent, and the whole of the new bonds to be deposited at St. Petersburg for ten years. The interest was paid regularly and the capital handed back in 1900.

The Great Discount Banks.—The Bank of France, although the most important, is not the sole dispenser of credit in France. Side by side, and always actively competing with it, have grown up such great institutions as the Crédit Lyonnais, the Comptoir National d'Escompte de Paris, the Société Générale, and the Crédit Industriel et Commercial. Some of these have London offices, and a reference to vol. i. p. 367 of the *Encyclopædia of Accounting* will show that many of these foreign banks have a very large capital entirely paid up, so that to a great extent they lend their own money.

The Crédit Lyonnais stands next the Bank of France as a financial institution. The total of its deposits and of its portfolio are even greater than those of the Bank. It has 26 agencies in Paris, 116 in the departments, 16 in the chief cities abroad, and agents all over the world. It is thus in close touch with the commerce of every nation, and is able, and willing, to finance many of their Governments. These banks, thanks to their greater liberty, attract large deposits upon low terms, and demonstrate that the bank cheque is able to compete with the note in ordinary times; but in times of trouble deposits are withdrawn, and it is then that the Bank of France comes forward with its immense resources.

The Crédit Foncier de France, or Mortgage Bank of France, is an institution founded in 1852 to conduct the business that its name implies. It lends up to 50 per cent of the value of real estate, and secures itself by a first mortgage. A regular banking business is also carried on. The Foncier has been of great assistance to growing cities by financing their

schemes of improvement and reproductive works. Its premium or prize bonds have become very popular, and usually fetch more than their par value, as buyers are stimulated by the hope of winning one of the prizes, which vary from 1000 to 100,000 francs, attached to their drawings.

For the purpose of assisting cultivators the Foncier started a Credit Agricole, which completely failed to perform what it was expected to do.

PRIVATE BANKS.—In addition to the incorporated institutions, France has a great many private banks. In large cities their customers are chiefly traders and manufacturers in certain lines of business; thus one bank may draw its business principally from the wine and spirit trade, another from drapers, etc. Thus the bank becomes well informed about its customers, and can exercise great discrimination in case of need. Their transactions are mostly very simple and include dealings on the Bourse. No detailed statistics of private banks are published.

PRIVATE SAVINGS BANKS, under Government supervision, number about 547, with 1299 branches, and deposits amounting to 3264 millions of francs.

POSTAL SAVINGS BANKS, introduced in 1881, hold deposits amounting to 1081 millions of francs.

BANKING IN HOLLAND

By the end of the sixteenth century the commerce of Holland had assumed a world-wide character, and Amsterdam had become an emporium for the products of Europe and the Indies alike. Naturally the merchants of divers nationalities who assembled there brought with them as many varieties of coinage of a very mixed character, in all stages of wear and tear. Sweating and clipping of coin were in those days only too common, so that, when all these circumstances were taken into account, settling became a rather complex and difficult matter. Gresham's law had a fine field for asserting its truth, and came into full operation accordingly. Its action was not fully understood in those days, but what was brought home to the commercial world was the fact that all the best and heavy coins mysteriously disappeared from circulation, while the light, worn, and clipped variety was painfully in evidence. This result was attributed to the money changers and dealers in specie, and rightly so, regarding them as the active instruments for executing Gresham's law. Bankers also came in for a share of the general censure, inasmuch as it was erroneously believed that bills of exchange as a substitute for money had also contributed towards the depreciation of the coinage. Accordingly in 1608-1609 bankers and money changers were suppressed. It was made punishable by heavy fines to hold deposits, or pay or receive money for another, and all persons were admonished neither to pay nor receive money at rates higher than the legal standard. Transfers and bills of exchange were also forbidden, but it was soon found necessary to relax some of these regulations. Meanwhile the city authorities had been maturing a plan for the establishment of a great institution which would undertake, under public control, the business of receiving deposits of cash and of dealing in specie; these ideas assumed a tangible shape with the foundation of the celebrated Bank of Amsterdam in January 1609. The regulations for its control were very simple. Any person might open an account with the Bank and deposit coin or bullion; he might then draw on his account and transfer sums to the account of another. These deposits could not be seized by legal process, and the remuneration of the Bank was one-fortieth of one per cent on deposits and withdrawals.

To duly appreciate the services rendered by the Bank it must be borne in mind that coins of all sorts and conditions, in addition to bullion, were accepted, duly appraised at the legal current prices, and credited accordingly. The credit as it stood in the books of the Bank was called *bank money.* Thus bank money was synonymous with full-weighted current coin, and it goes without saying invariably commanded an agio or premium as compared with the nondescript ordinary money of the period. Small change was discriminated against, it only being accepted to the extent of 3 per cent in the form of *schellingen.* Thus the very practice was perpetuated and accentuated which had previously been legislated against, as the public very soon distinguished between "bank money" and "ordinary money."

As time went on the Bank gradually departed from its original practice of merely receiving deposits and repaying them on demand, and finally got into difficulties through lending too freely to the East India Company. Public confidence in the Bank was lost, never to be regained, and it was closed by royal decree in December 1819.

Middleburg established a bank, similar to that of Amsterdam, in 1616, which lingered on after some changes till 1878; and Rotterdam established another in 1635 which gradually died out.

The later history of banking in Holland centres in the Bank of the Netherlands. Like the other great banks already discussed, it is a private institution, and is the only bank of issue ever established in the country. It was founded in April 1814 with the help of the Government, but for the first forty years of its existence made very little progress in any branch of banking. This is attributed to the fact that the practices of discounting and loaning had not as yet developed to any great extent in Holland. The Government also was not free from blame. The original charter did not permit the Bank to lend on foreign bonds, or discount bills bearing fewer than three signatures, and all loans had to pass through the hands of a notary. Later charters removed these restrictions.

The Bank, although established with the assistance of the Government, has always maintained a very independent attitude, even when the Treasury has been in actual need of funds. It has been charged with lack of zeal in the public service, and not without some show of reason; for though the first charter permitted branches to be established in various large trade centres, yet nothing came of it.

The second charter in 1838 directed the bank to open a branch in Rotterdam, but this was not done. When the time came for the renewal of the charter for a third period, many persons maintained that the Bank had not justified its existence, and should be suppressed, and that legislation should be enacted whereby any one might issue notes. The Dutch Government did not adopt these views, but at the same time they have been borne in mind, and the door is still open for a free banking system should it ever be deemed desirable to establish one.

The Act of 1863 renewed the Bank's charter for a period of twenty-five years.

Article 1 provided that no other bank of issue should be established, and no foreign bank should circulate notes except by special law.

Article 5 required the Bank to establish a branch at Rotterdam, and at least one agency in each province, besides appointing correspondents where needed.

The branch was duly established, and there are now 18 agencies and sub-agencies; there are also 48 first class, 14 second class, and 10 third class correspondents' offices.

The difference between an agency and a sub-agency is immaterial to the public. First and second class correspondents carry on a full banking business.

Third class correspondents merely collect bills and other documents, so that, omitting these and including the head office, there are 82 centres where bills are discounted, loans granted, notes cashed, issued for specie, or exchanged for others.

Article 7 limited the credit operations of the Bank to discounting commercial paper and granting loans on collateral. It was forbidden to lend on mortgage, on security of ships, or note of hand; nor might it purchase bonds or goods, but might invest its reserve in the national debt and in mortgage bank bonds.

The Act of 1863 forbade the Bank investing in foreign bills, whereas we have seen that bills on England are a special feature in the operations of the Reichsbank. This anomaly has now been removed.

The charter of the Bank came up for renewal in August 1888, when its capital was raised to its present figure of 20,000,000 florins; one-fifth of this may be invested in certain bonds, and foreign bills may be purchased.

The Bank reserve is regulated by royal decree upon application by the directors of the Bank. This was settled in April 1864, and has not been revised since.

A ratio of two-fifths is laid down between the metallic reserve on the one hand and the total cash liabilities on the other, *i.e.* note circulation, current bank bills, and deposits. Thus, presuming the note circulation amounted to 90 millions, current bank bills to 1 million, and deposits to 9 millions, then the metallic reserve should be 40 millions; but if it happened to be 45 millions then there would be a surplus reserve of 5 millions.

The present Bank charter dates from 1st April 1889, and expires on 31st March 1904; but, as provided by law, the Government has already given notice that it does not intend to continue the concession for another period without modification.

The affairs of the Bank are supervised by a Government official, and the king nominates the president and secretary.

Of the profits the stockholders first take 5 per cent on their capital. Of the balance 10 per cent goes to reserve until the fund has reached 5,000,000 florins. The remainder is equally divided between the Bank and the State, but when the shareholders have received a dividend of 7 per cent two-thirds of the balance remaining go to the State, and one-third to the Bank.

When requested the Bank must grant loans to the Government up to a total of 5,000,000 florins at the usual rate of interest upon security of Treasury notes, but this obligation is inoperative when the "surplus reserve" falls below 10,000,000 florins. Investments in foreign bills must not exceed the "surplus reserve" for more than fourteen consecutive days. Should the surplus reserve become reduced by exportations of coin and bullion, the Bank would be obliged to realise on its foreign bills, supposing their amount to have already reached the maximum, but, as a matter of fact, the foreign bills always fall short of the maximum, and the Bank continues in a position to go on lending.

The currency of the Netherlands consists chiefly of silver and paper. Before 1875 the country had a silver standard, but in that year a bill passed the States-General for the unrestricted coinage of gold 10 guilder pieces. The free coinage of silver was temporarily suspended in 1874, and again for an indefinite period in 1877. In addition to gold the silver coinage previous to 1875 is legal tender; the monetary system has been maintained at parity

by treating the large silver coins as redeemable in gold. They are now being minted gradually into small change for Holland and Java.

The Netherlands Bank furnishes gold freely for export, but sparingly for home circulation, and in this respect pursues a policy directly opposite to that of the Bank of France. The idea is to maintain a healthy state of foreign exchange, because the Bank is convinced that a refusal of gold for export would send the metal to a premium, and force a silver standard upon the nation. During the years 1880-84 the Bank's stock of gold was depleted in a most alarming manner, but thanks to prompt and drastic measures the danger was boldly met and averted. The Dutch monetary system proves that it is quite possible, within limits, to maintain a gold standard with very little gold, while the principal currency is silver and paper.

The Dutch standard coin is the 10 gulden piece, containing 6·720 grammes of gold $\frac{9}{10}$ fine, which gives as a par of exchange £1 = 12·11 gulden nearly. The silver florin, gulden, or guilder, weighs 10 grammes, ·945 fine. In addition to the ordinary circulation of the Bank of the Netherlands, to which there is no limit, there is an issue of Government notes of 10, 50, and 100 gulden to the amount of 15,000,000 gulden (£1,250,000). These are redeemable in cash at the Netherlands Bank, but the Government provides the necessary means in the shape of a "fund for ensuring the convertibility of Government notes against coin." This consists of 23,132,700 gulden inscribed in the register of the national debt.

There are one or two functions performed by the Bank which are extremely helpful to trade. In the first place, any person may obtain a bank bill for any amount, at any bank office, for a commission of 30 cents (6d.), in addition to the face value; and, secondly, persons having current accounts with the Bank may transfer or pay into each other's credit whatever sums they please free of charge; the customers need not reside in the same town. By these means transfers and payments to the extent of £35,000,000 annually are effected.

The Netherlands Bank, although the only note-issuing institution in Holland, is not the only banking corporation. There are many other firms or institutions engaged in one form of banking or another. In country places money is often placed in the hands of solicitors for investment. This is loaned to customers in their immediate circle, but a great proportion finds its way to Amsterdam, and is invested in the usual manner.

Banks of Deposit.—According to Dutch commercial law the business of a banker (*kassier* or *cashier*) consists solely in taking charge of money belonging to individuals or institutions, and repaying the same on demand. These cashiers, as they were called, have almost entirely disappeared, but there is at least one firm, the *Associate Cassa* of Amsterdam, which does business on the old lines. All its loans are made out of capital, or from deposits specially designated for that purpose. No other banks are conducted on this plan.

Dutch banks of deposit approach very nearly to the English type. Of the funds entrusted to them they only keep sufficient for till-money, the remainder being invested at call or otherwise, and all rely with confidence upon the facilities granted by the Bank of the Netherlands for obtaining credit. Their operations, if limited companies, are restricted to a great extent, for they may not grant loans on real estate or on note of hand, neither may they buy bonds for their own account except to a limited extent.

Other institutions use their resources in any way they think fit, and is is only in Amsterdam and Rotterdam that the genuine bank of deposit it

to be found. In those cities the banker is also the stockbroker, and sometimes the credit society or its agent.

The system of deposit banking is not yet very strongly developed in Holland, neither is the cheque so well known as in England. The bank note is used instead, and its circulation per head is the second largest in the world, that of France alone being greater. This shows that bank notes have an exceedingly wide range, and have not been superseded by other instruments of credit better adapted for economy in the use of coin.

CREDIT SOCIETIES (CREDIT-VEREENIGINGEN).—These are quite different from the German *Credit-vereine*, their business is on a large scale, and is not specially designed to satisfy the demand for small loans. The liability of each member is limited to the amount of his share, which is the maximum loan he can obtain by any means whatever. The society has its own capital, composed of the subscriptions of its members, which are (*a*) borrowing, and (*b*) non-borrowing. Each borrower must pay up a certain percentage of his share, and give his acceptance at three months or thereabouts; the society can then discount this at the Bank or elsewhere, and has thus another source to draw upon, together with deposits, which are accepted, and current account balances. These credit societies are establishing agencies, and are gradually spreading all over the country.

MISCELLANEOUS BANKS. — There are many other establishments in Holland which do not come under either of the above headings. Their operations are of a very wide nature, and include bills of lading, the purchase and sale of bonds, bills of exchange, and coupons. Financial commissions of all kinds are also undertaken, and many houses do a regular banking business.

POST OFFICE SAVINGS BANKS were established in 1881. Their functions are well known.

MORTGAGE BANKS also exist. They issue mortgage bonds, and thus procure the means to lend on real estate for long terms.

BANKING IN ITALY

HISTORICAL.—If England is the mother of parliaments, Italy is the mother of banks.

The Bank of Venice, usually considered to be the oldest bank, was founded in 1156 as a result of forced loans, whereby the State carried on its wars with the Roman Empires of the East and West.

These loans were converted into perpetual annuities, and Government Commissioners issued stock certificates to creditors, the bank being at this stage merely a transfer office for the national debt, which served certain purposes of exchange in those days, much as similar securities do now.

It was not until the latter part of the sixteenth century that deposit banking took its rise in Venice, when foreign coins were received at their bullion value, and certificates issued promising to pay an equal weight of bullion of the same fineness.

The Bank of Venice, as usually known, was founded by decree of the Senate in 1619.

In 1344 the Government of Florence owed about £60,000, and being unable to pay it, converted the whole into transferable stock, which was called a Mount or Bank (literally, a heap). Monte was the Italian term for a joint-stock fund, thus different Venetian loans were termed Monte Vecchio, Monte Nuovo, Monte Nuovissimo (old, new, newest). The Mont de Piété at Paris and Monte dei Paschi, a mortgage bank at Sienna, are

other examples of the use of the word. The Germans had considerable commercial relations with Northern Italy at this period, and their equivalent word was Banck, which was promptly Italianised into Banca; from this the English form is easily seen. In the early days of American finance a "bank" was invariably connected with the issue of a batch of paper money. The term was applied to the sum of money in contradistinction to the institution itself.

The wars of the fourteenth century led to the formation of the Bank of Genoa, while the multiplicity of Government creditors was the reason for founding the Bank of St. George in 1407, which became the State banker and financial adviser from that time forward.

The private bankers of the great cities of Italy were the original prototypes of modern loan and deposit banks; the Jews were the money-lenders of the dark ages, the business being left entirely in their hands owing to the Christian abhorrence of usury. Presently the Christians began to expel the Jews from one country after another, and then the Christian merchants of Lombardy and elsewhere began to remit money by bills of exchange and to lend at interest. The circulation of notes payable to bearer and redeemable on demand in coin was not developed until the time of the Bank of Amsterdam. The wars of Napoleon changed the boundaries of states, destroyed the freedom of the great cities of Italy, and brought most of the old banks to an end.

The first successful attempt to found a modern bank in Italy resulted in the Bank of Genoa, established in 1844 with a capital of 4,000,000 lire, in addition to which it received a Government subsidy of like amount, on which it paid 2 per cent interest. It was supervised by two royal commissioners.

The Bank of Turin was founded in 1847 with a capital of 4,000,000 lire, but the troubles of 1848 caused it to unite with the Bank of Genoa at the end of 1849, under the new title of "National Bank of Sardinia," with offices at Genoa and Turin.

In 1848 the Bank of Genoa lent the Government 20,000,000 lire, its notes were made forced legal tender, and its circulation increased by 20,000,000 lire; the loan was repaid and specie payments resumed next year. From this time the Bank became intimately connected with the fortunes of the rising kingdom of Sardinia, its sphere gradually extending with the successes of the royal arms.

It was reorganised in 1859 as the National Bank of the Kingdom of Italy, with an increased capital of 40,000,000 lire, and three coequal head offices in Genoa, Turin, and Milan respectively. Branches were established in many of the chief cities, in some cases absorbing the leading banks already existing there.

The conquest of the Two Sicilies did not result in the destruction of the Banks of Naples and Sicily, but several branches of the National Bank were planted in the southern portion of the newly consolidated kingdom.

It was not until August 1893 that the constitution of the Bank was radically changed, although it was compelled to enter into close relations with the Government, and accept forced legal tender for its notes in order to supply the State with funds. When the war of 1866 broke out specie payments were suspended, but forced legal tender applied only to the notes of the National Bank, which was also required to furnish notes to the other banks without charge.

It was the intention of the Government to unify the banking as well

as the political system of the kingdom, but existing rights were respected. No new bank was permitted to be established without special legislation, but there were five other banks of issue doing business side by side with the National Bank. These were the Bank of Naples, the Bank of Sicily, the National Bank of Tuscany, the Tuscan Bank of Credit, and the Roman Bank. They complained that they suffered on account of the special treatment accorded to the National Bank, and to remedy this the Consorzio was established in 1874.

By this arrangement the banks were formed into a syndicate for the withdrawal of Government notes and substitution of the notes of the National Bank, which were to be legal tender throughout the kingdom, while the notes of the other banks were to be legal tender only in their own provinces.

The associated banks were required to supply the Government with credit to the amount of 1,000,000,000 lire, a certain portion being in gold. The Consorzio came to an end in 1884, when forced legal tender was also abolished.

During 1892-93 the entire banking system of Italy almost collapsed. The crisis commenced with the suspension of specie payments and the failure of the Roman Bank. It was found that most of the banks had illegally increased their circulation with the connivance of public officers, and had locked up their funds in investments not easily realised. Upon investigation it was ascertained that huge sums had been paid to Ministers, deputies, and others, either as gifts or ostensible loans. When the full extent of the disaster had been ascertained, it was seen that a clean sweep of the old system could not be avoided, and the occasion was seized as a further step in the policy of consolidation.

The new law of August 1893 provided for the amalgamation of the National Bank of the Kingdom of Italy with the National Bank of Tuscany and the Tuscan Bank of Credit. The new institution was called the Bank of Italy, but there is no Bank of Italy in the same sense as the Bank of France, the Bank of the Netherlands, and the kindred institutions of England and Germany.

The Roman Bank had already passed away; thus there remain in Italy three great banks of issue—the Bank of Italy, the Bank of Naples, and the Bank of Sicily.

The former was required to establish branches wherever those of the National Bank of Tuscany previously existed. The capital was fixed at 300,000,000 lire, and its privileges confirmed for twenty years. The maximum limit of circulation during the continuance of forced legal tender was 800,000,000 lire for the Bank of Italy, 242,000,000 for the Bank of Naples, and 55,000,000 for the Bank of Sicily. By 1907 these sums must be reduced to 630,000,000, 190,000,000, and 44,000,000 respectively; and each bank must possess a reserve equal to one-third of its circulation, failing which the circulation must be reduced within three months, and the amount of the reduction transferred to the banks which possess or pay in the necessary reserve.

The authorised circulation may be increased provided the excess be covered by legal coin or gold bullion; it may also be increased for the purpose of lending to the Government.

The reserves of the banks when on a specie basis are fixed at two-fifths of the circulation, composed of one-third coin or bullion, and the remainder in approved foreign bills. At least three-fourths of the metallic reserve must be in gold.

Banks of issue are permanently supervised by the Ministers of Commerce and the Treasury, who make a special inspection every two years, and report to Parliament within three months.

The new banking law did not remedy the evils of a depreciated currency, and the Government was again obliged to issue more paper in order to supply its pressing needs. In January 1894 the Bank of Italy was permitted to issue an additional 90,000,000 lire, the Bank of Naples 28,000,000, and the Bank of Sicily 7,000,000; the penal law on these issues was reduced to two-thirds of the rate of discount.

A month later the circulation of State notes was limited to 600,000,000 lire, and the banks were allowed to redeem their notes on demand at their market value, provided that they transferred 200,000,000 lire in gold to the credit of the Government, and accepted a fresh issue of Government notes instead; but the volume of outstanding notes was not reduced, and the gold withdrawn from the banks was not replaced. Such financiering merely intensified the deplorable state of the currency, and what the Government gained on the one hand it lost on the other by increased adverse rates of foreign exchange and diminished gold value of the Treasury receipts.

As an expedient to protect the Treasury the coupons of the national debt were taxed 20 per cent, which was simply another way of reducing the interest from 5 to 4 per cent.

The depreciated paper drove even the subsidiary coinage out of circulation, which found its way principally to France and Switzerland. At one period it was found that over 40 per cent of the French subsidiary circulation consisted of coins of other States composing the Latin Union, but mainly Italian. Means were taken for sending back these coins, and the Italian Government, in order to prevent its silver from again straying abroad, locked it up in the Treasury and issued small notes against it.

A special inquiry into the condition of the banks gave but faint hopes of the restoration of a healthy state of affairs, but an attempt in this direction was embodied in the arrangement of February 1895, which the Bank of Italy was practically obliged to accept.

By its terms the banks were allowed fifteen years in which to realise their unavailable assets, and the Bank of Italy undertook the winding up of the Roman Bank, receiving for its services, after giving certain guarantees, the custody of provincial public funds. Sums above 40,000,000 lire were to bear interest at 1½ per cent. The Bank was to deposit 50,000,000 lire in national securities with the Treasury as a guarantee fund, and after six years to increase the amount to 90,000,000 lire; at the same time advances to the Government were to be increased from 90,000,000 to 100,000,000 lire. Shareholders were required to pay up a further sum of 30,000,000 lire on their shares, and to reduce the capital by a like amount. As a reserve fund to cover losses by the Roman Bank, the sum of 4,000,000 lire was to be set aside in 1894, 5,000,000 lire in 1895, and afterwards 6,000,000 lire annually; any profit remaining might be divided among the shareholders to the extent of 40 lire per share.

The Schulze-Delitzsch co-operative institutions of Northern Italy are a special feature of the national banking system. Their capital consists of the paid-up shares of the associates, who must hold at least one each, and complete their subscriptions within three months. A society is worked by meetings of its members formed into various committees, such as the Council of Administration, the Discount Committee, and Committee of Experts.

Ordinary commercial paper is discounted, and advances made upon

warehouse warrants. The society also grants loans on honour only, without security, to persons of good reputation who have a trade or shop, and are recommended by two sponsors. The maximum amount of a loan under these conditions is 100 lire, repayable by weekly instalments.

In Southern Italy the three great banks of issue pursue an equally beneficent course towards small traders, cultivators, and even labourers. The law of 1887 also permitted them to grant loans for agricultural purposes.

But the people's banks obtain a very valuable privilege from the great banks, inasmuch as they can get their commercial paper rediscounted by them at very low rates. The Bank of Naples rediscounts at 1 per cent below its usual rate, and the Bank of Sicily deals with the people's banks in an equally liberal manner.

On the other hand, the great banks find that they are in a great measure relieved of the difficulty of discriminating between the different classes of paper offered them. The officials of the popular banks have such a wide knowledge of their borrowers, that their paper is selected with extreme care, fraud is rare, and practically impossible. The relationship between the two is very similar to that existing between the London bill brokers and their patrons the big banking corporations.

In the year 1899 there were 818 co-operative credit societies and popular banks in Italy, in addition to 158 ordinary credit companies, and eleven establishments of the Credit Foncier. Post Office Savings Banks, established in 1876, numbered 5233, and there were 464 private Savings Banks, all subject to Government regulation and supervision.

The deposits in the Post Office Savings Banks amounted to 628,000,000, and in ordinary banks to 1,431,000,000 lire.

It is pleasant to record that the strenuous efforts put forth by the Italian Government during the past few years with the object of restoring the finances of the country are meeting with great success. It is a striking fact that in 1895 the circulation of the three great banks of issue amounted to a grand total of 1,055,000,000 lire, which sum was reduced in 1900 to 471,000,000 lire. The following extract from a recent issue of the *Financial News* (July 1903) gives an admirable summary of the present situation:—

"For some years past the material conditions prevailing in Italy have undergone steady and almost uninterrupted improvement. The natural resources of the country have been systematically developed, old industries have been revived and modernised, and new industries have been successfully established especially in the northern and central districts. Economies of a far-reaching character have been introduced and insisted upon, alike by the Government and by the more go-ahead of the local authorities, and in place of serious deficits in the public finances year after year, recent budgets have shown balances on the right side. The result has been seen in a marked advance in Italian credit and in the value of Italy's securities.

"Less than a decade ago Italian Rentes stood at about 71; they have since risen to well over par; and the fact that the exchange on London and Paris, which not many years ago involved a loss of fully 16 per cent to Italian traders, has steadily fallen to the normal level is an especially favourable feature in the economic condition of the country."

Banking in Japan

Paper money was used in Japan from a very early period, but its modern history may be said to date from the overthrow of the feudal

system in 1868, when the Mikado assumed full control of the government of the country. In order to pay the indemnities granted to the feudal lords as compensation for the surrender of their ancient rights, it was considered advisable to continue the circulation of the existing paper money; this was presently followed by a new and improved issue which attained to a still wider circulation than the old.

The birth of the banking system of Japan may be traced to the establishment of "exchange houses" in many parts of the country in 1869, but these did not prosper, and the next step was the establishment of National Banks under the Government National Bank Regulations of 1872, which followed rather closely the National Bank system of the United States.

The legislation of 1872 was intended chiefly to maintain the value of the Government paper money, the redemption of which was partially provided for by the issue of Government stock. Banks were required to secure their circulation with stock, the notes being redeemable in gold on demand; but this was soon found to be impracticable on account of the persistent depreciation of silver and the excess of paper.

Thereupon the National Bank regulations of 1872 were hastily remodelled in 1876, the banks being authorised to redeem their notes in Government paper. Bank capital was allowed to take the shape of any kind of Government stock, which was to be deposited with the Treasury in return for 80 per cent of the amount in circulating notes.

The next five or six years saw a great increase in the number of banks, which, including branches, numbered 260 in 1880; but the state of affairs continued to grow worse. Paper fell 40 per cent below silver in value, and 50 per cent below gold, while a further issue of Government paper to pay the cost of putting down the rebellion of 1877-78 merely aggravated monetary conditions.

An immediate effort was made to restore something like order in the financial system by the suspension of further issues of paper, and the issue of short-term interest bearing Treasury bonds redeemable in Government notes, in addition to long-term 7 per cent bonds redeemable in silver. A certain portion of these bonds were redeemed by annual drawings, and an equal quantity of paper money burnt. Measures such as these have always proved efficacious under similar conditions, and the usual result followed here.

Having got rid of the incubus of the feudal system the domestic industry of Japan soon broke forth into foreign exports, which gave rise to inpouring streams of foreign silver in return. Banks bought up the depreciated paper in such quantities that the issue of bonds was curtailed lest a deficiency of currency should follow. Specie was received by the Customs at its current value in paper, which a few years later was quoted in the neighbourhood of par.

It was in 1881 that Count Matsukata Masayoshi assumed the supreme control of the finances of Japan. A few years before, when Vice-Minister of Finance, he had successfully initiated a system of private ownership of land, combined with land taxation and a conversion of the hereditary pensions of the warrior class into bonds. It may well be imagined that the Count was by no means satisfied with the existing order of things, it being the great aim of this "financier of the first order" to set the banking and monetary system of his country upon a firm and enduring foundation.

His travels in Europe and America, and his close observation and study

of the various systems of the West, admirably qualified him for the task, the results of which, together with a description of the means whereby these results were attained, he has embodied in his *Report on the Adoption of the Gold Standard in Japan*, from which much of the information contained in this article is extracted.

As already stated, the modified system of 1876 was hasty, and therefore imperfect. The existing banks were comparatively small and situated in circumscribed localities, their business relations were of the most meagre description, and *esprit de corps* there was none. A state of affairs was possible in which one bank might hold an ample surplus, while its neighbour was in dire need; but mutual assistance was neither expected nor afforded.

The Minister of Finance of the day felt that adjustment of the Government paper was needed, and that to do this satisfactorily a great central bank was necessary, which should also be invested with the sole privilege of issuing convertible bank notes.

It would also serve as the supreme organ for regulating the currency of the country, for discounting bills of exchange in order to regulate the influx and efflux of specie and bullion, and for performing certain services for the Treasury so as to simplify the business of the Exchequer.

It was contended that a big central bank, if established, would—

1. Facilitate the circulation of currency throughout the country.
2. Be able to supply capital to National Banks, as well as to trading and manufacturing companies.
3. Lower the current rate of interest, because it would increase the supply of loanable capital.
4. Transact Government business to the advantage of the Government, and establish foreign correspondence.

Accordingly, the Bank of Japan (Nippon Ginko) was founded on October 10, 1882, with limited liability and a capital of 10,000,000 yen, since increased to 30,000,000 yen. The head office is situated in Tokio, with eighteen branches elsewhere, and its charter runs for thirty years. Its shares are all registered, and only Japanese subjects may hold them. Shareholders must be approved by the Minister of Finance. The management of the Bank is entrusted to a governor, vice-governor, and four directors; there are also from three to five auditors.

The first notes issued by the Bank were redeemable in silver on demand, and it was by their instrumentality that the disparity between silver and paper money disappeared in 1886.

The Bank was allowed an uncovered circulation of 85,000,000 yen, of which not more than 27,500,000 yen were to replace bank notes cancelled after 1887.

The German "elastic limit" was also adopted, together with the accompanying tax of 5 per cent upon excess issues; but of course the circulation might be increased to any extent when covered by specie. The circulation not covered by specie must be covered by good commercial paper or Treasury bonds.

The Act of 1883 provided for the retirement of the notes of the local banks at the expiration of the twenty years for which they were chartered by means of funds deposited with the Bank of Japan. The charters of the banks ran out between 1896 and 1899, and by December of the latter year Treasury notes and National Bank (Kokusitsu Ginko) notes were withdrawn from circulation. The paper money now in circulation consists of Nippon Ginko notes, or notes of the Bank of Japan, which are redeem-

able in gold on demand; their circulation on April 1, 1902, amounted to 187,194,336 yen.

In December 1900 there were in existence in Japan 2534 banks of various kinds, having 2213 branches.

Of these the common banks numbered 1802, with 1374 branches, and deposits amounting to 437,000,000 yen.

The Savings Banks numbered 681, with 814 branches, and 29½ millions of deposits. These banks must be joint-stock and have a capital of not less than 30,000 yen. One-half the paid-up capital must be deposited with the Treasury in the shape of Government bonds as a guarantee fund for deposits.

During the official year 1900-1, 2,335,173 persons deposited 39,434,012 yen, and withdrew 14,700,563 yen from the post offices, which also act as savings banks.

The YOKOHAMA SPECIE BANK, with its eighteen branches, ranks next to the Nippon Ginko. It was founded in February 1880 with the object of discounting bills drawn on foreign countries, so as to afford banking facilities to importers and exporters. It originally issued bank notes secured with bonds convertible into specie.

Its capital consisted of 1,000,000 silver yen in shares held by the Government, in addition to 400,000 silver yen, and 1,600,000 paper yen held by private shareholders.

As the value of silver differed widely from that of paper, and constantly varied, separate accounts had to be kept for the two, and these presented so many difficulties that the bank was entirely reorganised in July 1887 with a capital of 18,000,000 yen, all of which is paid up.

The HYPOTHEC BANK OF JAPAN was founded in 1897, and is the chief mortgage bank of the country. This form of banking is evidently popular, as local hypothec banks have since been formed to the number of about fifty, with a paid-up capital of 30,000,000 yen.

A CREDIT MOBILIER was established in February 1902, its capital of 10,000,000 yen being subscribed three times over. Apparently it has a very successful future before it.

THE GOLD STANDARD.—The return of Count Matsukata to power in 1895 was marked by another great reform. The adjustment of the paper currency accomplished in 1886 prepared the country to reap the advantages of a scientific coinage. The rate of interest had become low, commerce and industry began to expand, but Japan was still a silver country, and had now to contend with a steady and continuous depreciation of the white metal.

Guided by the history of the Latin Union and the experience of other countries, the Count at once attacked the problem with the courage and sagacity for which he is renowned, and was quick to discern the benefits that would follow the adoption of a gold standard.

He accordingly prepared and carried in 1896 the measure which established the present gold standard in Japan. It was a fortunate coincidence that during the period in which the change was being effected the price of silver was almost stationary, so that prices were undisturbed, and the burdens of debtors unaffected. Since the adoption of the gold standard Japanese bonds sell well in the London market, and the rapid progress made by the country in every branch of trade gives great cause for satisfaction, and amply proves the wisdom and discernment of the great financier.

The present monetary law of Japan dates from October 1897. The unit of value is the yen, which is not coined, but is equivalent to exactly 0·75 grammes of pure gold. The coined metal is $\frac{9}{10}$ fine, and the coins minted are

the 20-yen piece, weighing 16·666 grammes, its least current weight being 16·575 grammes; the 10-yen and the 5-yen piece of proportionate weight.

The gold coins formerly issued were of 20, 15, 10, 5, 2, and 1 yen respectively. They contain twice as much gold as the new coinage of the same denomination, hence they circulate at twice their face value. This fact should be carefully noted. The old 1-yen piece weighs 25·72 grains. Since the sovereign contains 7·32238 grammes of pure gold, we deduce a mint par of exchange with Japan of 1 yen = 24·58 pence. Gold coins are, of course, legal tender to any amount, and worn coins having suffered only fair wear and tear are exchanged free of charge.

Silver coins are legal tender for sums not exceeding 10 yen, and bronze up to 1 yen.

The 1 yen silver coin has been withdrawn from circulation. The silver coins now current are the 50 sen, 20 sen, and 10 sen. The 50-sen piece weighs 208 grains $\frac{8}{10}$ fine, the other coins weighing in proportion.

The 5-yen piece is of nickel. The bronze coins are the 1 sen and 5 rin. 10 rin = 1 sen, and 100 sen = 1 yen (or dollar).

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R. H. CARY.

APPENDIX

Note to "Banking in Holland," p. 72, sec. 8.

IN accordance with the law recently passed (October 1903) by the Dutch States-General, the privilege of the Bank of the Netherlands, which was to expire on 31st March 1904, has been extended until 31st March 1919, when it may be renewed from year to year.

The Bank consents to act, without any remuneration, as the banker of the State, the Postal Savings Banks, and the State Insurance Bank, in exchange for which services it is entitled to issue notes of the value of 25 florins and less, but not of a lower value than 10 florins. These notes will be brought into circulation in proportion to the withdrawal of the 50 florin and 10 florin Treasury notes now in existence, in which task the Bank will assist the Treasury until 1st October 1904.

As the total amount of Treasury notes in circulation is estimated at 15,000,000 florins, the Bank, at the request of the Minister of Finance, will have to grant advances to the Treasury up to 15,000,000 florins on the guarantee of such notes. This obligation, however, will lapse as soon as the State resumes the issue of paper money.

FOREIGN EXCHANGES

By ARCH. B. CLARK, M.A.

Foreign Exchanges.

Meaning of the Term

In technical usage the term "foreign exchanges" means the rates of exchange at which foreign payments are made, or, in other words, the prices of foreign bills of exchange, these bills being the medium through which the mutual indebtedness of nations is normally discharged. This is the sense in which the term is used when we speak of the exchanges rising or falling, being for us or against us. But in a wider sense it may be taken to denote the system under which international debts are settled by means of bills of exchange; and it is only by examining the nature and working of this particular department of the credit system that we can understand the conditions determining the prices of foreign bills or the rates at which exchanges are made.

Nature of the Transaction

In its most general form the position is admirably stated by Viscount Goschen:—"That which forms the subject of exchange is a debt owing by a foreigner and payable in his own country, which is transferred by the creditor or claimant for a certain sum of money to a third person, who desires to receive money in that foreign country, probably in order to assign it over to a fourth person in the same place, to whom he in turn may be indebted" (*Theory of the Foreign Exchanges*, p. 2). We may suppose, for example, that, as the result of international commerce, one group of French merchants, A, owes British merchants, B, a certain sum, while another group of French merchants, C, is entitled to receive on the same day from other British merchants, D, an equal amount. Then the loss in freight, insurance, and interest involved in the double transmission of bullion in settlement of these debts will be avoided if A pay C while D pays B. This is practically effected by the use of bills of exchange. C, for example, may draw bills on D for the amount owing, and through the medium of the brokers sell these bills to A, who will send them to B, by whom in turn they will be presented through the medium of the brokers to D for payment. In this case D's debt is said to be drawn for, and A's to be remitted for. If on the other hand we suppose that to effect a settlement B draws on A and sells to D, who remits to C, we have A's debt drawn for and D's remitted for.

Remitting and Drawing

By the custom of trade the great bulk of the foreign indebtedness to this country is remitted for, only a small percentage being drawn for. In other words, the bills drawn abroad on this country far exceed those drawn here on foreign countries. This custom is attributed to the operation of those causes that have combined to make London the world's "clearing-house." Owing to the enormous volume of our foreign trade and investments, the stability of our gold standard, and the great credit of the London houses, good bills on London are always in demand. The drawing and negotiation of the bills being thus for the most part effected by the foreign merchant it follows that, with a few exceptions, such as the Indian exchange, the rates of exchange between London and foreign cities are fixed abroad. The London quotations are for the most part adjusted to the telegraphed foreign quotations. By this custom the gain or loss arising from exchange fluctuations accrues to the foreigner; and this accounts for the comparative indifference with which such movements are regarded in this country, where the majority of merchants—selling for sterling to be paid in bills on London—have not, save indirectly through the reaction on the rate of discount (*v. inf.* p. 89), any interest in exchange fluctuations.

Real Par and Mint or Nominal Par

If, as assumed in the example given above, the debts due by the two countries to each other were in every respect equal—that is, equal in amount and of equal credit, payable on the same date and in the same currency—then there would be nothing to cause fluctuations in the price of foreign bills. The exchange between the two countries would be at par. But we have no means of knowing whether the indebtedness on each side at any given time is equal. This real par is therefore purely ideal. The mint or nominal par, on the other hand, is the expression of a concrete fact determined by the mint regulations of the two countries. By these regulations one English sovereign contains approximately the same amount of fine gold as 25·22½ francs, or 20·43 German marks, or 4·86⅔ United States dollars. This mint par is thus the result of a comparison of the legal weight and fineness of the coins of the respective countries, and is in no way dependent on the actual condition of the currencies. It can be altered only by a modification of the law defining the standard coin in one or other of the countries concerned. About this nominal par the exchanges fluctuate owing to inequalities in one or more of the four elements already mentioned.

Rise and Fall, Favourable and Unfavourable, Specie Points

It is convenient to begin by confining attention to one of these causes of fluctuation—the balance of indebtedness. Suppose, for example, that the debts payable by France to England on a given date exceed those due by England to France, *i.e.* the balance of indebtedness is against France and in favour of England. Then, under these circumstances, there will be in Paris an excess of demand for bills on London, by people having payments to make there, over the supply of such bills, since relatively few have payments to receive there. The exchange will turn against Paris and in favour of London. In other words, to avoid the trouble, risk, and expense of sending bullion, those who have payments to make in London (*e.g.*, French importers) will compete for bills on London. To obtain these they will offer more than their nominal value, *i.e.*, bills on London will rise to a

premium, or more than 25·22½ francs will be paid in Paris for a bill for £1 payable in London. In this case the exchange is said to have risen above par; and this may go on till the export specie or gold point is reached, *i.e.* till the party having the payment to make in London finds that it will pay him better to incur the expense of sending bullion than to buy a bill at the existing rate.

Similarly, if the balance is in favour of France and against England, there will be in Paris an excess of supply of bills on London over the demand for such bills. The exchange will turn against London and in favour of Paris. In other words, to get rid of their bills, the sellers (*e.g.* French exporters) will offer them at less than their nominal value, *i.e.* bills on London will be at a discount, or a bill for £1 payable in London will fetch in Paris less than 25·22½ francs. Here the exchange has fallen below par. But, again, this fall cannot go beyond the gold-import or specie point, *i.e.* the point beyond which it would better pay the party having the payment to receive in London to incur the expense of bringing home bullion to Paris than to sell his bill.

The expense involved in sending £1 between London and Paris differs slightly in different cases, but it may be taken as approximately 10 centimes. When therefore the exchange rises to 25·32½ a movement of bullion will take place from Paris to London, while a fall to 25·12½ will cause it to be shipped from London to Paris. Twice the cost of transmitting bullion is thus the utmost range of exchange fluctuations, when these fluctuations are due solely to changes in the balance of indebtedness, and not to differences in the time which must elapse before the bills have to be met, or to the state of credit or of the respective currencies.

The Course of Exchange—Interpretation of "Rise" and "Fall"

Whether a rise in the exchange is to be taken as favourable, and a fall as unfavourable, or the reverse, depends on the manner in which the exchange is quoted. In the quotation the currency unit of one country must be taken as the fixed term, and the number of units of the other currency that exchange for it as variable. In the example of the London-Paris exchange already discussed the pound sterling is taken as fixed, and the number of francs given for it as variable, and a rise in the exchange is seen to be a movement against Paris and in favour of London. But had the franc been taken as the fixed term and the number of pence given for it as the variable, a rise in the exchange would have meant a movement against London and in favour of Paris.

Now, which currency is taken as the fixed term depends on custom. On the Continent the usual practice is to quote all exchanges in terms of the home currency, *i.e.* the currency of the country in which the bill is negotiated, the foreign currency unit being taken as the fixed term. Thus France quotes all in francs, Italy in lire, Holland in florins (guilders), Germany in marks. Under this system a "rise in the exchange" means invariably a rise in the price of foreign bills, or a movement in the exchange *against* the home country. But in Portugal and in most extra-European countries this rule does not obtain. In some of these all the exchanges are quoted, not in terms of the home currency, but in terms of the currency of the country on which the bill is drawn. Thus Buenos Ayres, Monte Video, and Valparaiso quote in pence, francs, or marks for one peso. But in other cases the same place adopts different principles with different exchanges. New York, for example, quotes London in

dollars for £1 sterling, but Paris in francs for $1. Again, Lisbon and Rio quote Paris in reis for one franc, but London in pence for one milreis. In this case a rise in the Paris exchange is against Lisbon, while a rise in the London exchange is in favour of Lisbon.

In London, as a rule, for convenience of comparison, the exchange is quoted in the same terms as it is quoted abroad. To this rule there are three exceptions—the United States, the Spanish, and the Russian exchanges. In New York the exchange on London is given as already noted in dollars for £1, but London perversely quotes New York in pence for $1. St. Petersburg and Madrid formerly quoted London in pence to the silver rouble and duro respectively, and London still adheres to this practice, though St. Petersburg now quotes London in roubles for £10, and Madrid quotes London in pesetas for £1. But with these exceptions the general rule is as stated above, and under it the London rates of exchange fall into two groups.

(A) In the one group the pound sterling is taken as the independent unit or fixed term, and the amount of foreign currency—*e.g.* the French francs, German marks, or Dutch florins, for which it exchanges—as the dependent quantity or variable price. This group includes all the European exchanges except the Russian, Spanish, and Portuguese.

(B) In the other group the foreign currency unit—*e.g.* the Russian rouble, Spanish duro, Portuguese milreis, United States dollar, or Indian rupee—is the fixed term, and the variable is the number of British shillings and pence given for it. This group includes most of the extra-European exchanges, as well as those of the three European countries mentioned above.

The country or place the currency of which is taken as the independent unit is said to *receive* the variable price, and the place the money of which forms the dependent quantity is said to *give* the variable price. Thus London receives from Paris, Berlin, or Amsterdam, and gives to Lisbon, Calcutta, or New York.

In the case of the first group (A), a "rise in the exchange" means a fall in the price of foreign bills. Thus, if the Berlin exchange *rises above par* bills on Berlin are at a discount, or £1 will purchase a bill for more than 20·43 marks, and the exchange is *for* or *favourable to* London, and *against* or *unfavourable to* Berlin. Conversely a "fall in exchange" means a rise in the price of foreign bills. If, for example, the Paris exchange *falls below par*, bills on Paris are at a premium, or £1 will purchase a bill for less than 25·22½ francs, and the exchange in this case is against London and in favour of Paris. Thus all exchanges in which London *receives* the variable are favourable when above par and unfavourable when below par.

In the case of the second group (B), on the other hand, a "rise in the exchange" means a rise in the price of foreign bills. Thus if the American exchange *rises above par* bills on New York are at a premium, or more than $49\frac{5}{16}$d. must be given for $1, showing that the exchange is unfavourable to London. If, on the other hand, the Spanish exchange falls below par bills on Spain are at a discount, or less than 47½d. will be given for a duro, and the exchange is favourable to London and against Spain. All exchanges in which London *gives* the variable are thus seen to be favourable when below par, and unfavourable when above par.

It appears, therefore, that the interpretation of "rise" and "fall" depends on which currency unit is taken as the fixed term, and which as the variable price.

The following tables from the *Economist* of 11th April 1903 show (1) the

London course of exchange; (2) the discount quotations in the leading cities; and (3) the foreign rates of exchange on London:—

London Course of Exchange

On	Usance.	Prices Negotiated on 'Change. April 2.	Prices Negotiated on 'Change. April 7.	
Paris	Cheques	25 16¼ 25 21¼	25 16¼ 25 21¼	= Francs and centimes for £1
Do.	3 months	25 37½ 25 42½	25 37½ 25 42½	
Marseilles	,,	25 37½ 25 42½	25 37½ 25 42½	
Amsterdam	At sight	12 2¾ 12 3¼	12 2¾ 12 3¼	= Florins and stivers for £1
Do.	3 months	12 5 12 5⅛	12 4⅞ 12 5⅜	
Berlin	,,	20 66 20 70	20 65 20 69	= Reichmarks and pfennigs for £1
Hamburg	,,	20 66 20 70	20 65 20 69	
Frankfort	,,	20 66 20 70	20 65 20 69	
Vienna and Trieste	,,	24 23 24 33	24 23 24 33	= Florins and kreutzers for £1
Antwerp	,,	25 38¾ 25 43¾	25 38¾ 25 43¾	= Francs and centimes for £1
St. Petersburg	,,	241⅜ 241⅝	241⅜ 241⅝	= Pence for 1 rouble
Moscow	,,	24¾ 24⅞	24¾ 24⅞	
Genoa, Naples, etc.	,,	25 47½ 25 57½	25 48¾ 25 58¾	= Lire and centesimi for £1
Madrid, Barcelona, etc.	,,	34¾ 35	34¾ 35	= Pence for 1 peso
Lisbon	,,	41 11/16 41 15/16	41⅝ 41⅞	= Pence for 1 milreis
Switzerland	,,	25 40 25 45	25 40 25 45	= Francs and centimes for £1

The discount quotations current in the chief continental cities are as follows. [London bank rate, 4 per cent; market rate, 3 7/16 per cent]:—

	Bank Rate. Per Cent.		Open Market. Per Cent.
Paris	3	May 24, 1900	2 13/16
Berlin	3½	Feb. 12, 1903	2⅜
Hamburg	3½	Feb. 12, 1903	2⅜
Frankfort	3½	Feb. 12, 1903	2⅜
Amsterdam	3	June 20, 1901	3⅜
Brussels	3	June 20, 1901	2¼
Vienna	3½	Feb. 6, 1902	2¾
Rome	5	Aug. 27, 1895	4
Turin	5	Aug. 27, 1895	4

	Bank Rate. Per Cent.		Open Market. Per Cent.
Genoa	5		4
Geneva	3½	Mar. 12, 1903	3¼
St. Petersburg	4½	Mar. 13, 1902	nom.
Madrid	4	Sep. 11, 1902	3
Lisbon	5½	Jan. 11, 1899	5
Stockholm	4½	Jan. 9, 1902	4
Christiania	5	Dec. 1902	5
Copenhagen	4	Feb. 6, 1902	4

At other centres the latest recorded quotations are:—

	Per Cent.		Per Cent.
New York (call money)	5	Calcutta, Bank min.	6
Do. (endorsed bills)	5¾	Bombay, Bank min.	7

Foreign Rates of Exchange on London

	Latest Dates.	Rates of Exchange.	Usance.
Paris	April 8	25·17	Cheques
Brussels	7	25·21½	,,
Amsterdam	7	12·13	Short
Berlin	7	20·51	,,
Do.	7	20·30½	3 months
Hamburg	7	20·50	Short
Frankfort	8	20·49½	,,
Vienna	8	23·99	,,

Foreign Rates of Exchange on London—continued

	Latest Dates.	Rates of Exchange.	Usance.
St. Petersburg . .	April 7	94·05	3 months
New York . . .	8	4·83⅝	60 days' sight
Lisbon	7	42⅜	,,
Madrid	8	34·09	,,
Italy	7	25·17½	...
Rio Janeiro . . .	6	12 1/32 d.	90 days' sight
Buenos Ayres . .	6	48¾d.	,,
Do. Pm. on Gold	8	127¼	...
Montevideo . . .	Mar. 14	52⅛d. Bng. Sng.	90 days' sight ...
Melbourne . . .	20	¾ dis. ½ pm.	60 days' sight
Sydney	20	¾ dis. ½ pm.	,,
Adelaide . . .	20	¾ dis. ½ pm.	,,
Calcutta . . .	April 8	1/3 31/32	Telegraph transfer
Bombay . . .	8	1/3 31/32	
Hong Kong . . .	8	1/7 11/16	Transfer
Shanghai . . .	8	2/2⅛	,,

The following are the standards for gold points of the principal gold exchanges:—

Francs. FRENCH.	Marks. GERMAN.	Dollars. AMERICAN.
25·32½—4 per mille for us	20·52—5 per mille for us	4·89—5 per mille for us
25·22½—Par	20·43—Par	4·867—Par
25·12½—4 per mille against us	20·33—5 per mille against us	4·827—8 per mille against us

The latest exchanges are:—

French "cheque" exchange . . . 25 f. 17 c., or 2¼ per mille against us.
German short exchange . . . . 20 m. 51 pf., or 4⅜ per mille for us.
New York Exchange "Cable transfers" . $4.87¼, or 1¼ per mille for us.

In published lists such as this only the variable prices are given, a knowledge of the fixed terms being assumed. In the twofold quotation given in the London course the better rate is that for first-class bank-paper, the worse that for ordinary trade bills. But whether the better or worse rate stands first depends on how the exchange is quoted, *i.e.* whether in sterling or in foreign money.

From the preceding discussion it is evident that a favourable exchange is favourable to buyers of foreign bills, *e.g.* importers, and *ipso facto* unfavourable to sellers of such bills, *e.g.* exporters. And in this connection it is worthy of notice that the exchanges are unfavourable when, *ceteris paribus*, there is an unfavourable balance in the mercantilist sense, *i.e.* an excess of imports over exports. So far the expressions "favourable" and "unfavourable," as applied to the exchanges, appear as a survival from a time when mercantilist ideas prevailed, an example of "fossil history." But apart altogether from this historical mercantilist interpretation, the use of these epithets may be justified from the modern standpoint in view of the influence of the state of the exchanges on the bank reserve and the rate of discount. A favourable exchange inclines towards the import specie-point. It is favourable in the sense that an inflow of gold means an increased reserve and a fall in the rate of discount, which in turn tends to induce an expansion of credit, rising prices, and commercial activity. An unfavourable exchange, on the other hand, tends towards the export specie-point. It is unfavourable inasmuch as it threatens a foreign drain of gold with consequent

diminished reserve, rise in the rate of discount, contraction of credit, falling prices, and depression of trade.[1]

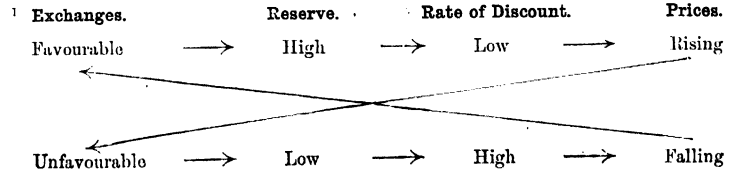
It is to be observed, however, that the course of exchange may be favourable to this country, while yet there is an "unfavourable balance" in the mercantilist sense. The balance of trade is only one of many elements that go to determine the balance of indebtedness; and this in turn, as already indicated, is but one of the causes affecting the course of the exchanges, on which depends the inflow or outflow of bullion.

Causes of Fluctuations in the Exchanges

I. International Indebtedness.—The primary cause of fluctuation is to be found in the relative indebtedness of the two countries concerned. The reference here, however, is not to permanent indebtedness, but to the debts payable on the date in question. All the world is debtor to Great Britain, but, apart from the periodical payment of interest, the magnitude of this foreign indebtedness will not move the exchanges by a hairbreadth in favour of this country till the time of the payment approaches. It is true that if the payment of any large sum is known to be impending the influence of this on the exchanges will be anticipated just as the price of wheat is affected by estimates of the probable outcome of the next harvest. The prices of bills, like the prices of commodities generally, are affected by men's forecasts of the future relations of demand and supply. But allowing for this, it may be said that the balance of indebtedness which affects the exchanges depends on the debts which fall due and must be settled, and not on those that are in abeyance. The elements that go to determine the balance of indebtedness may be grouped thus:—

(1) *Trade Indebtedness*, i.e. *Material Imports and Exports.*—It is clear that a country is a debtor to other countries to the extent of the value of its imports, and a creditor for the value of its exports. The former, therefore, tell against the balance, the latter in favour of it. Not only are these the most important items in the national balance-sheet, but, as hitherto assumed, they may be taken as typical of all the others. These others may, indeed, be reduced, in so far as their influence on the exchanges is concerned, to terms of imports and exports.

(2) *Loans to and Investments in Foreign Countries.*—These, at the time they are made, act on the balance, and therefore on the exchanges like imports into the lending and exports from the borrowing country. The lending country becomes a debtor for the time being by importing securities for which it must pay in goods or in gold. Only when the former prove inadequate, and bills in consequence rise above the specie-point, will the latter means of payment be adopted. The borrowing country, on the other hand, exports securities, and is creditor till it receives the proceeds of the loan. To contract a foreign loan has the same effect on the exchanges as an increase of exportation; and provided it can be done, it is the simplest method of correcting an adverse exchange. The sale of large holdings of foreign stocks will tend in the same direction.



(3) *Interest on Foreign Loans and Investments and Repayment of such Loans, as well as all Donations and Tributes from Abroad.*—These tell in favour of the balance of the creditor country just as exports do. The interest annually received by Great Britain on the immense sums lent to or invested in her own colonies, the United States, and other foreign countries, is estimated to amount to upwards of £90,000,000. This tells in favour of England's balance, and goes, together with the annual remittances of the American Irish to their kindred in the old country, and the remittance home of savings by India civil servants and others, to swell the annual volume of imports the United Kingdom is entitled to receive.

(4) *Freights, Commissions, Brokerages, etc.*—A country is a creditor for the carrying work done by its ships on behalf of foreigners, and also for the commissions earned by its bankers, brokers, and agents who transact business for foreigners. In the case of imports the freights form part of the price paid by the home consumer, but the freight on the exports is ultimately paid by the foreign consumer. The element of freight has been aptly described by Sir R. Giffen as an "invisible export." Now our ships do the greater part of the world's carrying trade, and it is estimated that the United Kingdom earns in freights £70,000,000 annually (*v.* Giffen, *Essays in Finance*, 2nd series, pp. 171-89). As regards banking and commission business it is clear from London's position as the settling house of the world that the amount falling due annually on this account must also be very large.

The causes discussed under heads 3 and 4 account for by far the greater part of the annual excess of imports over exports of material commodities in the case of the United Kingdom.

(5) *Expenses of Foreign Residence, Government Political and Military Expenses Abroad, etc.*—These tell against the balance of the country incurring such expense. The expenses of absentee Irish landlords must be met by exports from Ireland. So also part of America's excess of exports goes to defray the expense incurred by Americans travelling in Europe. This is also an important factor in the Russian exchanges. "The bills drawn by the travelling princes on their St. Petersburg bankers affect the exchanges precisely with the same force as bills drawn on St. Petersburg for the champagne sent thither from France" (Goschen, *Theory*, p. 20). As much may be said of political and military expenditure. Adam Smith's words are apposite to-day. "The enormous expense of the late war, therefore, must have been chiefly defrayed, not by the exportation of gold and silver, but by that of British commodities of some kind or other" (*Wealth of Nations*, bk. iv. ch. i.)

Such are the leading constituent elements of international indebtedness, the comparative amount of which is the primary cause of exchange fluctuations. It is evident that the necessary condition of continued solvency for any nation is that its imports must be paid for by exports—taking these terms in their widest sense as including securities, freights, commissions, and all forms of immaterial as well as material commodities. A nation, it has been seen, may temporarily restore the equation of indebtedness and "correct" an adverse exchange by borrowing abroad. For the time being it exports securities; but this simply means that in the long-run it must export more in the shape of material commodities or services.

So far as international indebtedness is the sole operating cause, the variation in the exchanges is limited, as already explained, by the specie-points. But there are other influences to be considered which cause

fluctuations beyond these limits. Of these there now falls to be considered the element of *time*. Differences in the time which must elapse before the bills become payable constitute, as indicated earlier in this article, a cause of exchange fluctuations. This arises from its bringing into play the influence of the rate of interest, and allowing greater scope for the influence of the state of credit in determining the price of foreign bills.

II. The Rate of Interest.—(*a*) The rate in the country where the bills are drawn is occasionally important. A high rate affects the exchanges, "since it renders the seller more eager and the purchaser more reluctant." The former is anxious to obtain cash, while the latter hesitates to lock up cash. Thus in America in 1861, when the Civil War was impending, there was a favourable balance of trade—*i.e.* there had been great exports to, and comparatively few imports from Europe. Therefore, the other elements in the balance of indebtedness—*e.g.* interest on loans—not being equivalent to this excess of exports, there was an excess of supply in New York of bills on London. The price of bills on London might, therefore, have been expected to fall to specie-point. But on this occasion in America, owing to the collapse of credit, the urgent demand for ready cash, and the expected high rate of interest, capitalists hesitated to lock up their capital, and the exchange on London fell far below specie-point. This, however, is a case of an exceptional type, as it is rare to find a stringent money-market co-existing with a favourable balance of indebtedness (*vide* Goschen, *Theory*, pp. 48-52).

(*b*) The rate of interest in the acceptor's country—the country on which the bills are drawn—is more generally important. It is the primary cause of difference in price as between "long" and "short" bills. In the preceding discussion it has been assumed for simplicity that all bills are drawn payable at sight. But practically the great majority of bills are drawn payable so many days after date or after sight. Generally the "usance" varies from thirty days to six months, according to the custom of the trade. Now the difference in price between say a sight bill and a three months' bill consists, *ceteris paribus*, of interest, reckoned at the rate prevailing in the place on which the bill is drawn—the bank rate of discount in the case of trade bills, and the market rate in the case of first-class bank-paper. By this amount the long-rate will be lower than the sight-rate if reckoned in the currency of the drawing country, higher than the sight-rate if reckoned in the foreign currency (*vide* Clare, *A B C*, chap. xii.)

It is to be noted here that bills on London are bought in Paris, Berlin, or New York not merely for remittance in payment of debts, but for investment. First-class bills of exchange are the most convenient form of investment for that part of the banker's money which he requires to keep in a readily available shape, since he can speedily replenish his store of ready money by simply letting his bills run out without restocking his portfolio. London bankers, it appears, do not invest largely in foreign bills of exchange. They confine their purchases to home bills. But foreign bankers do invest very largely in bills on London. Now, as regards the purchase of such bills for remittance in payment of a debt, the higher the rate of interest in London the more, *ceteris paribus*, will the foreign buyer be willing to give for a "short" bill, and the less for a "long" bill on London; for with the former, if his debt is payable immediately, he averts the necessity of paying the high rate of interest, and with the latter he must either pay the high rate till the bill becomes due, or cash it at the high rate of discount. The position is similar with regard to the purchase of foreign bills as an interest-yielding investment. Three months' bills on

London are bought in Paris say at the "long" or cheaper rate, and sold when due at the "short" or dearer rate, the difference being the return in interest. The higher, therefore, the rate of discount in London when the bill is bought, the greater, *ceteris paribus*, the margin of difference between the prices of "long" and of "short" bills, the better, consequently, the prospect of profit if the rate is expected to remain high, and the greater the demand for bills on London. Thus a rise in the London market rate above the market rate in Paris will at once tend so far to move the exchange in favour of London. A rise in the London bank rate alone will not suffice for this, since the foreign banker will buy for investment only first-class bank-paper, and the interest allowed for in the price of this is, as already indicated, not the bank rate, but the market rate. In a time of stringency, however, the market rate will follow the bank rate. When the money market is "easy" and the bankers' reserves are high, the market can and does undersell the bank, and a rise in the bank rate is ineffective. But in times of stringency, when money is scarce, the "other deposits" with the Bank of England, *i.e.* the bankers' reserves, are low; and the discount houses, relying themselves on the Bank of England for aid, cannot afford to undersell it. At such a time, therefore, the bank rate rules the market. Hence a recognised mode, and in this country the standard mode, of "correcting" the exchanges, turning them in favour of London, and so checking a drain of gold and replenishing the reserve, is to raise the bank rate.

But apart from its immediate influence on the price of bills, the rate of discount affects the exchanges through its influence on the state of credit and the condition of trade. A low rate tends to produce, in course of time, an expansion of credit, increased speculation, rising prices, and an increased importation both of securities and commodities. This, other things equal, leads to an adverse balance and an unfavourable exchange, which again reacts on the reserve and the rate of discount. A high rate, while at once attracting gold from abroad, as we have seen, or at least checking the drain, at the same time leads directly to a contraction of credit at home, and a fall in prices of securities and commodities with an increased exportation of both, and a resulting favourable balance.

III. The State of Credit is a powerful cause of fluctuations in the exchanges. In the absence of good credit a rise in the rate of interest, however great, will be unavailing as a "corrective" to an unfavourable exchange, for there will be no investment demand for bills on the country in question. Even where the credit of a country is normally high, as is that of England, it has happened in times of panic that the rise in the rate of discount has proved ineffective. Thus in 1866, the year of the crisis marked by the failure of Overend, Gurney, and Company, the bank rate in London stood for upwards of three months at 10 per cent, or 6 per cent above the Paris rates. Yet the Paris exchange remained for the whole time against London. On the other hand, owing to skilful management the Baring crisis of 1890 left the credit of England and the rate of exchange with European capitals practically unaffected. In connection with the state of credit the element of time, as already observed, is important. It accounts often for differences in the rates of exchange quoted for "long" and for "short" bills—differences which cannot be explained by differences in the rates of interest ruling in the places in question. There is more risk of failure on the part of the drawer or acceptor in the case of a three months' bill than in that of a bill at sight; and the greater the

risk, the greater is the margin of difference between the "long" and the "short" exchange.

IV. THE STATE OF THE CURRENCIES IN THE EXCHANGING COUNTRIES.—Owing to the operation of the causes already considered, it is clear that fluctuations in the exchanges may take place even when the countries concerned have the same currency system. But the liability to as well as the scope of fluctuation is much increased by differences in the relative value of the currencies in use. To take a classical instance, before the foundation of the Bank of Amsterdam in 1609 that city had become flooded with clipt and worn foreign coin, and good money was no sooner issued than by the operation of Gresham's law it was driven from circulation. Hence there was great uncertainty as to the value of bills on Amsterdam, and the exchange was always against her. To remedy this state of matters—to meet the need for a good currency in which foreign bills might be paid—the bank was established. It received the actual currency at its metallic value, and after deducting expense of recoinage, etc. gave credit for this in its books. This credit was called bank money, and, as it represented money of the mint standard, it was always worth more than current money. Payment of foreign bills was to be made in bank money, and this removed all uncertainty as to their value. (See Adam Smith, *Wealth of Nations*, bk. iv. ch. iii.)

(*a*) *The Paper Exchanges.*—But the most striking illustration of the influence of currency differences on the exchanges is seen where the currency of the one country consists of gold and that of the other of inconvertible paper depreciated through discredit or from excessive issue. In such a case the exchanges, if quoted in terms of the depreciated currency, appear very unfavourable to the paper-using country. This, however, is the *nominal* exchange. To obtain the exchange in terms of bullion or the *real* exchange, it is necessary to deduct the premium on gold. The best example at present is the Argentine Exchange. Owing to the depreciation of the Argentine currency, the premium on gold at one time stood as high as 300 per cent, *i.e.* the paper peso had fallen to one-fourth of its nominal gold value.[1] But nearly every civilised country has at one time or other had experience of inconvertible paper. In England, during the suspension of specie payments (1797–1821), the notes of the Bank of England were issued in excess. As a consequence a premium on gold appeared, and the exchanges became unfavourable to England. America had a similar though worse experience under the *régime* of inconvertible "greenbacks" (1862–1878), when a premium on gold of 285 was recorded. The existence of such a depreciated inconvertible paper currency is, it is hardly necessary to observe, a serious impediment to trade. Fluctuations in the premium can never be foretold. A merchant in England, for example, may sell goods to a customer in Argentina for a certain paper price, and instruct his customer to remit a bill for that amount. But before the remittance reaches him the premium on gold may have risen, and his bill will fetch so much less. He may, doubtless, sell for gold, or make forward exchange contracts, but that merely shifts the risk, and he pays for the insurance. Similarly a merchant in Argentina selling goods in London for a certain price will suffer if the premium falls before he can sell his bill.

In the case of exchange between gold standard and inconvertible paper standard countries, therefore, it appears that the limit to the nominally

[1] In the quotation for Buenos Ayres given above (p. 90), the rate of exchange of the gold peso in pence is stated together with the gold premium, from which the rate in terms of paper can be deduced.

adverse exchange is specie-point, plus the premium on gold plus insurance against a rise therein.[1] If there is no gold, then the limit to the adverse movement is commodity-point. In other words, if the country having inconvertible paper has been drained of its stock of gold, then the price of bills on it may fall till it would better pay to bring commodities from it than to sell a bill.

(*b*) *The Silver Exchanges.*—Similar reasoning to the above is applicable to the case of the exchanges between gold standard and silver standard countries. Here in seeking to find the real state of the exchange from consideration of the nominal exchange allowance must be made for variation in the gold value of silver. There can be no *mint par* of exchange save between countries having the same standard of value. But before 1873, when the gold-price of silver was fairly steady at a little over 60d. per ounce, there was a stable par of exchange about which the actual exchanges fluctuated within narrow limits. But when the fall in the gold-price of silver began that stable par disappeared. The fall was in its nature fluctuating and uncertain, and, like the depreciation of inconvertible paper, it acted as a serious impediment to trade. Of this type of exchange the Anglo-Indian was formerly the leading example. But with the closure of the mints of India to the free coinage of silver in 1893, the rupee ceased to fluctuate in its gold-price as silver fluctuated. The rupee is now maintained by the application of the principle of limitation at the fixed gold price of 16d., or R.15 = £1. In other words, India is for exchange purposes a gold standard country, and the exchange between England and India fluctuates like other gold exchanges within the comparatively narrow limits set by the specie-points. The Mexican and Chinese are now the leading examples of the silver exchanges.

The Effects of Currency Depreciation and Appreciation on Foreign Trade

It may be taken as a general principle that every rise in the price of foreign bills so far tends to stimulate exports, since it enables the exporter to obtain a better price for his draft; conversely, every fall in the price of foreign bills tends to stimulate imports, since it enables the importer to buy his remittance in payment at a cheaper rate. A specific depreciation of paper or of silver, that is, a rise in the paper-price, or silver-price, of gold, will tend therefore to stimulate exports from the paper-using or silver-using country to the gold-using country, and to check exports thither from the gold-using country. This deduction has been amply borne out by experience. The Mexican export trade flourishes with the fall in the gold-price of silver, for the exporter, sending his goods to London, can, so long as he gets the same gold-price, or one which has not fallen in proportion to the fall in the gold-price of silver, sell his sterling bill for more Mexican dollars, while his expenses at home have not risen. The same is true of the Argentine exporter so long as the general level of paper-prices in Argentina has not risen. But, conversely, the exporter from the gold-using country suffers, since, obtaining only the old silver or paper-price for his goods, his bill will now sell for less gold. It is only during the process of depreciation, however, that there is any stimulus or check. Once general paper-prices have risen in Argentina in proportion to the rise in the paper-price of gold the influence on trade disappears. The same is true of the

[1] The specific depreciation of a country's currency will *ceteris paribus* show itself in a fall or rise in the foreign exchanges according as it *receives* or *gives* the variable.

exchange with silver-using countries, save that as experience shows the readjustment may be made by a fall in gold-prices rather than by a rise in silver-prices.

Where the depreciation of the currency is not a specific depreciation relatively to gold, but a general depreciation, *i.e.* where paper-prices generally rise through over-issue before the paper-price of gold rises, the stimulus and check respectively will be in the opposite directions to the foregoing. The merchant in the gold-using country sending his goods to the paper-using country will obtain the higher paper-price, which on conversion at the old ratio will fetch more gold. The merchant in the paper-using country, on the other hand, gets for his exports to the gold-using country only the former gold-price, which, converted at the old ratio, fetches only the old paper-price, while his expenses in paper have risen. But again this stimulus and check can only last till the premium on gold equals the general depreciation of the notes (*vide* Nicholson, *Money and Monetary Problems*, 6th ed. p. 369).

Indirect Settlement of Indebtedness—Arbitration of Exchange

Hitherto the existence has been assumed of two countries dealing exclusively with each other, and the operations discussed constitute what is known as "direct exchange." But in practice the results are modified, and extreme variations in any particular exchange are in general prevented by the close interconnection existing between all the chief commercial countries. There are, for example, instances of "triangular trade," such as the trade of the United States, China, and England. The United States pays for her excess of imports from China by remitting bills drawn on London against her excess of exports thither, the indebtedness of London to China thus created being met by England's normal excess of exports to that country. "Indirect exchange" will be resorted to in the settlement of debts whenever the difference in the rates of exchange is such that even a very small margin of profit can be secured by so doing. Thus the Paris banker who wishes to remit to London may not remit direct if the London exchange is against Paris. He may find that the Berlin exchange is favourable to Paris, and that the exchange between Berlin and London is favourable to Berlin. In that case it may pay him to purchase, and remit to London bills on Berlin. This constitutes *simple arbitration* through Berlin.

More circuitous transactions are what is known as *compound arbitration*. Suppose, for example, that in Paris bills on Amsterdam are pressed for sale, and the Paris banker learns that in London bills on Amsterdam are in demand, while bills on Berlin which are scarce in Paris are superabundant in London. Then the Paris banker may see his way to make a profit by purchasing and remitting to London bills on Amsterdam, and instructing his London correspondent to send him in return bills on Berlin.

Thus in the absence of disturbances due to the state of credit the competition of bankers in the arbitrage business tends to prevent any considerable divergence between the rates for bills of the same kind in different markets.

AUTHORITIES.—Goschen's *Theory of the Foreign Exchanges;* Clare's *Money-Market Primer and Key to the Exchanges;* also the same writer's *A B C of the Foreign Exchanges.* This last is now the best work for students, though Goschen's exposition of principles remains unsurpassed. There are excellent chapters on the subject in Bastable's *Theory of International Trade* (4th ed.), Nicholson's *Principles of Political Economy*, vol. ii., and Pierson's *Principles of Economics*, vol. i. Tate's *Cambist*, 23rd ed., is the standard work of reference for the details of exchange operations.

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INDEX

THE END

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